SPECIAL REPORT
SEPTEMBER 28, 2009 | BUSINESSWEEK.COM

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100 Best Global Brands

PLUS

The Great Trust Offensive

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The McGraw-Hill Companies


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Consumer trust is more important than ever, says McDonald's Mary Dillon

SPECIAL REPORT

100 BEST GLOBAL BRANDS

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(COVER) TYPOGRAPHY BY SEB LESTER; (ABOVE) MICHAEL L. ABRAMSON



President Calderon may have to ax three ministries

PUMMELED BY PEMEX

After years of surpluses, Mexico is facing a growing budget gap. The government's most pressing question: Can it reduce dependence on oil? BW | PAGE 036



SUBPRIME REDUX?

Developers are jumping on a little-known program at the Agriculture Dept. that offers home mortgages with 0% down. To some, that raises red flags BW | PAGE 028

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Jack and Suzy Welch are off while Jack recovers from a back infection

(L TO R) ANDRE PENNER/AP PHOTO; ILLUSTRATION BY THOMAS FUCHS


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THE BUSINESS WEEK

EDITED BY HARRY MAURER & CRISTINA LINDBLAD



A Beijing tire plant: The U.S. slapped a 35% tariff on Chinese-made tires

(FROM TOP) NIR ELIAS/REUTERS; JIM WATSON/AFP/GETTY IMAGES

ECONOMICS & POLICY

A TIFF OVER TIRES

Sometimes you just have to keep your people happy. That seems to have been **President Barack Obama's** calculation when he approved, on Sept. 11, a 35% tariff hike on Chinese tire imports for three years, though there's no indication that China is dumping the tires below cost. Why would Obama risk inflaming tensions with a major trade partner? Because the original beef was brought by the **United Steelworkers,** the dominant union in U.S. tire plants and a key ally in Obama's battle to pass health-care reform. Beijing predictably made outraged noises and on Sept. 14 filed a complaint with the **World Trade Organization,** arguing that the tariffs are unjustified. For good measure, Beijing suggested it may bring dumping charges against U.S. poultry and auto parts in China. Some analysts worry that the conflict could cast a pall over a late September U.S. visit by **Chinese President Hu Jintao** as part of a **Group of 20** summit in Pittsburgh. The concern seemed validated by Beijing's rapid-fire retaliation, which did not indicate much sympathy for Obama's domestic political pressures. But Chinese officials soon signaled that they'd prefer a negotiated solution rather than a tit-for-tat trade war.

SHOPPERS VENTURE OUT

U.S. consumers decided in August that it was safe to hit the malls—or at least tiptoe back in. The **Commerce Dept.** on Sept. 15 said retail sales excluding automobiles increased by a better-than-expected 1.1% from July. As for cars, the cash-for-clunkers program helped inflate sales by 10.6% from the previous month, while gas station revenues were up 5.1%, largely because of pricier gasoline. Other numbers, too, suggested more juice running through the economy, as Fed chief Ben Bernanke noted in calling the recession "very likely over." Overall producer prices jumped 1.7% in August, though they remain 4.3% below their year-earlier

2.7%

Rise in U.S. retail sales in August, the biggest increase in three years

Data: Commerce Dept.

level, and the consumer price index rose by a hefty 0.4%. The year-over-year decline in CPI eased to -1.4%, vs. -1.9% in July.

A BILL BUSINESS LIKES

The Gang of Six delivered at last, and their health-care bill may be the one business favors. After months of talks with five of his **Senate Finance Committee** colleagues, **Senator Max Baucus** (D-Mont.) issued his proposal on Sept. 16. It leaves out the controversial publicly financed insurance plan contained in a House bill, but it would require nearly all Americans to buy health insurance starting in 2013, with subsidies for families making $66,000 a year or less. Baucus would levy fat new fees on insurers, medical device makers, clinical labs, and drugmakers to help underwrite the cost of the bill, estimated at $856 billion over 10 years.

THE COST OF HEALTH

And what if Congress doesn't come through with sweeping health-care reform? Annual health costs for business will soar 166% over the next decade, to $29,000 per worker, says the Business Roundtable. That's even worse than the prior decade, when costs shot up 131%.

"Skyrocketing Employer Health-Insurance Premiums" businessweek.com/magazine

OBAMA ON THE STREET

On Sept. 14, the first anniversary of the failure of **Lehman Brothers, President Barack Obama** came to Wall Street—but not to deliver an elegy. Instead, he pledged to push through reforms he proposed in June to prevent another meltdown. The measures include expanding the Fed's powers, creating a consumer financial protection agency, and giving Washington the clout to break up troubled firms. Most of the proposals are extremely unpopular on the Street, evidenced by the fact that not a single CEO of a major bank was in the audience. The President warned against a return to "reckless behavior" and exhorted the industry to "embrace serious financial reform, not fight it." Congressional action is expected in the fall.

| BW | PAGE 023 "Financial Innovation Under Fire"

FINANCE

GO TO TRIAL, BOFA

Bismarck famously said that legislation, like sausage, is



Obama speaking at Federal Hall: The audience wasn't exactly enthusiastic

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something you never want to see made. Maybe he should have included corporate mergers as well. One whose back room drama and possibly dodgy details are about to be laid bare for all to see: last year's **Bank of America-Merrill Lynch** deal. On Sept. 14 a federal judge rejected for the second time a $33 million settlement BofA had reached with the **SEC** over charges that it negligently failed to provide its shareholders with details about Merrill's true financial picture before they voted to approve the deal. In his ruling, **U.S. District Court Judge Jed Rakoff** said the settlement victimized shareholders again, since the fine would effectively come out of their pockets. Rakoff set a Feb. 1 trial date, a move that is likely to result in a public airing of the maneuvers that preceded the deal.

| BW | PAGE 066 "Do Shareholder Class Actions Make Sense?"



Back in 2007, *BusinessWeek* broke the story about "life settlements"

CORUS GETS CORRALLED

If you've ever wanted to own a waterfront condo in Miami, you do now—along with the rest of us. On Sept. 11 federal regulators seized Chicago-based **Corus Bank,** which continued to pump money into condo projects in south Florida in 2006 and 2007 even after other lenders had backed away. Regulators had ordered Corus to boost its reserves, then gave the $9 billion bank until mid-June to raise capital or find a buyer. But with bidders unable to value the bank's vast portfolio of vacant or unfinished condo projects, the feds moved in. Other banks deep in commercial real estate could make up the next wave of failures.

'DEATH BOND' WATCH

The Wall Street Journal on Sept. 16 reported that the **SEC** has created an "agencywide task force" to study so-called life settlements: financial products that allow consumers to sell their life-insurance policies to investment firms, which continue paying the premiums and collect the payouts when the people die. In a July 30, 2007, cover story, *BusinessWeek* warned of the dangers of the fast-growing market and sounded alarms about Wall Street's efforts to turn the deals into securities. "The investment banks are wading into murky waters," *BusinessWeek* wrote. "The life settlements industry increasingly finds itself in the grip of dubious characters devising audacious and in some cases illegal schemes to make money."

PANG PASSES AWAY

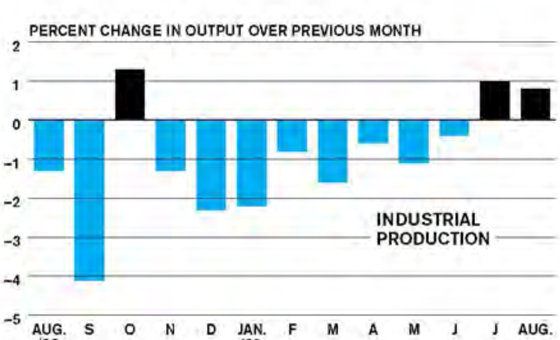
Danny Pang, the financier accused by the **SEC** of running a massive Ponzi scheme, died on Sept. 12 after being found unconscious in his Newport Beach (Calif.) home. A county coroner said there was no evidence of foul play and that toxicology tests could take two to three months. Pang, 42, was charged with fraud in April. The complaint said he raised hundreds of millions from Taiwanese investors, promising them guaranteed returns from life insurance and real estate time shares.

STRATEGY

WOOING JAPAN AIRLINES

One might wonder why several of the world's major airlines seem to be scrapping for a

BACK IN POSITIVE TERRITORY



Data: Federal Reserve



JAL maintenance: The ailing airline is cutting 6,800 workers

HARUYOSHI YAMAGUCHI/BLOOMBERG NEWS



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minor stake in a money-losing carrier that's in the process of cutting 6,800 workers. Among the parties involved in talks about a cash infusion of up to $300 million in Japan Airlines: **American Airlines** parent **AMR, Air France-KLM,** and **Delta Air Lines.** A successful bidder would grab greater access to Asian markets and likely some of the landing slots JAL controls at Tokyo's **Narita** airport. JAL has been on the government dole, having received three bailouts since 2001, and is working against a recession that will cause the global airline industry to lose $11 billion this year, said the **International Air Transport Assn.** on Sept. 15. Its cash quest comes as the U.S. and Japan work on finalizing an "open skies" treaty this year, which could lead to expanded airline alliances and joint ventures in trans-Pacific flights.

LEADERSHIP

ELEVATED AT INTEL

Who'll get to be top dog? Intel on Sept. 14 outlined a new structure that puts three executives in the running to succeed **CEO Paul Otellini** in a few years. **Executive Vice-President Sean Maloney** will head up the core **Architecture** group, which handles chip design and marketing. **Dadi Perlmutter,** another executive vice-president, will direct product development. The **Technology & Manufacturing Group** will be headed by **former CFO Andy Bryant.** Gone in the shuffle is **Pat Gelsinger,** who co-headed the lucrative enterprise computing unit. On Sept. 14 data storage outfit **EMC** named Gelsinger president and COO of information infrastructure products.



A shuffle at Intel puts three executives in the race to succeed CEO Otellini

IDEAS WILL CALIFORNIA'S GREEN STYLE WORK ELSEWHERE?

California's finances are in a shambles, and its politicians are perpetually feuding. Yet when it comes to green policy the Golden State still stands out as a model—not just for the rest of the U.S., but also for the world. So argues **Ronald Brownstein** in the October issue of *The Atlantic*. Brownstein points out that the state's role as "an environmental pace-setter" goes all the way back to the 1940s, when it became the first to establish air pollution controls. In the oil crisis in the early '70s, California was at the forefront of efforts to promote energy conservation. And the Obama Administration used as the basis for nationwide regs a 2002 California law that for the first time curbed tailpipe emissions of carbon dioxide and other greenhouse gases.

One of California's big lessons, says Brownstein, is that regulations can create markets. The state captured nearly three-fifths of the $3.3 billion in venture capital that flowed into clean-tech statups last year—companies making a range of goods from solar panels to electric cars. Yet even Brownstein acknowledges that the California approach may not be easy to replicate in other parts of the country. The combination of a temperate climate, an economy not heavily reliant on power-intensive heavy industry, and households that are smaller than the national average all give California a leg up in the quest for energy efficiency.

▶ *The Atlantic*



Solar panels in California: The state has long been a green pioneer

(FROM TOP) JUSTIN SULLIVAN/GETTY IMAGES; MICHAEL GOULDING/THE ORANGE COUNTY REGISTER/ZUMA PRESS

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(TOP) BRAD TRENT; (BOTTOM) JEFF HUTCHENS/REPORTAGE BY GETTY IMAGES

UNION LEADER ANDY STERN ON THE FUTURE OF BIG LABOR

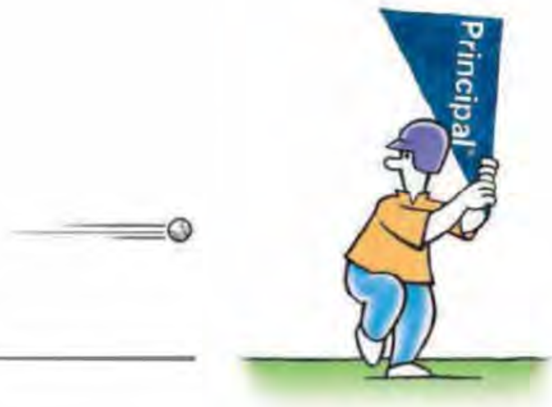
As *BusinessWeek* went to press on Sept. 16, the AFL-CIO had elected Rich Trumka as the new leader of the federation, succeeding longtime President John Sweeney. Trumka would be heading a much larger organization if Andy Stern, head of the Service Employees International Union, had not taken his union (now 2.1 million strong) out of the AFL-CIO four years ago. Stern, once a student at the Wharton School, was an early critic of banking industry practices and the private equity juggernaut. He is passionate about health reform (about 1 million members of the SEIU are health-care workers), and he is a staunch supporter of President Barack Obama. The SEIU, according to *The Wall Street Journal*, was also a generous backer of the voter registration group Acorn (the Association of Community Organizations for Reform Now), which is under fire for allegedly unethical behavior recorded on videos by conservative activists.

MARIA BARTIROMO

Could the election of Trumka lead to a re-merger between the SEIU and the AFL-CIO? Should business be worried?

ANDREW L. STERN

The good news is that the AFL-CIO and all the unions have been pretty united when it comes to health care



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SCOTT GOLDSMITH/AURORA

Trumka, the new head of the AFL-CIO, as he was being nominated in Pittsburgh

and free choice [eliminating the secret ballot in union elections].

Didn't taking your union out of the federation four years ago diminish the power of Big Labor?
No. I think it's allowed a healthy discussion about whether unions really want to be lapdogs of a political party or watchdogs for the interests of the members and their families. If we can all come back together with a new plan, that would be very exciting.

What led to the bad blood between you and the AFL-CIO? At one point, you were one of Sweeney's top lieutenants.
American workers were losing their health care, their jobs, their long-term security. The rich were getting richer. And we were not willing to change in spite of all that American workers were confronting. So when you're walking down a road and you know where it ends, the wise thing to do is walk in a different direction where there's hope. Rich Trumka has a real opportunity here to work together to [fix] what I think we all now acknowledge is a labor movement that needs to change.

An op-ed in the *Journal* on Sept. 16 says the SEIU gave Acorn $7.4 million between 2005 and 2008. Do you still support Acorn?
We have been watching this story unfolding with concern, and we have encouraged [Acorn] to take dramatic steps to resolve the underlying problems. Some of the behaviors we've seen on the videos are unacceptable.

Are you disappointed with the attention President Obama has given to issues of importance to labor?
Between the economy, wars, and the lack of hope, no one has been left in such a deep hole at the beginning of their Presidency. Getting out of it is going to take time. So we're just going to have to be patient, collaborative, thoughtful, and do what has worked well in health care, which is build coalitions with employers and organizations that normally haven't worked together. With health care we've demonstrated, by working with the Business Roundtable, the Federation of Independent Business, Intel, and Wal-Mart, that there are certain issues that are not Democratic or Republican issues—they're American issues.

So what would you like health-care reform to look like?
I would like a system where there are no more cases like Pat DeJong, who lost her husband and then, because of the medical bills, lost the ranch that had been in her family for 100 years. We need insurance reform where there's no excessive out-of-pocket expenses or restrictions on preexisting conditions. We need to cut costs and make sure there's real competition, because there are many states where one insurance company dominates the market and the prices are higher than in other parts of the country. And we need to make sure everyone takes part in the system, as they do with car insurance.

Long before the economy collapsed, you were a critic of the banking industry and private equity. What are your thoughts as we watch the financial industry being put back together?
First of all, we were right that there was an irrational enthusiasm that we could just make money by leveraging companies, creating debt, securitizing it, and the world would never end. Anybody who has to balance their budget appreciates that you have to create worth and live within your means if you're going to be successful. The private equity model was a dead end. And [private equity has] shown they can't manage any better—which was their claim—than anyone else. So we need a new regulatory system and a financial framework that can't presume anyone is too big to fail. Also, I don't think it's a good idea for private equity to be buying into banks.

MANAGING FORWARD
THE RESET ECONOMY
Getting ready for the post-recession world

Has the recession led you to rethink the way you operate your union? What is the SEIU doing to prepare for a recovery?
Well, it's made us appreciate that we have to be better partners with our state governments and employers in terms of efficiency. It makes us appreciate that our pension funds are tied to the success of the economy. And it makes us very much want to come together with other Americans and employers and people in the nongovernmental part of our country and say we need to create a 21st-century American economic plan so Team USA can compete and win. |BW|

Maria Bartiromo is the anchor of CNBC's Closing Bell and writes the blog, Maria Bartiromo's Investor Agenda, at investoragenda.cnbc.com

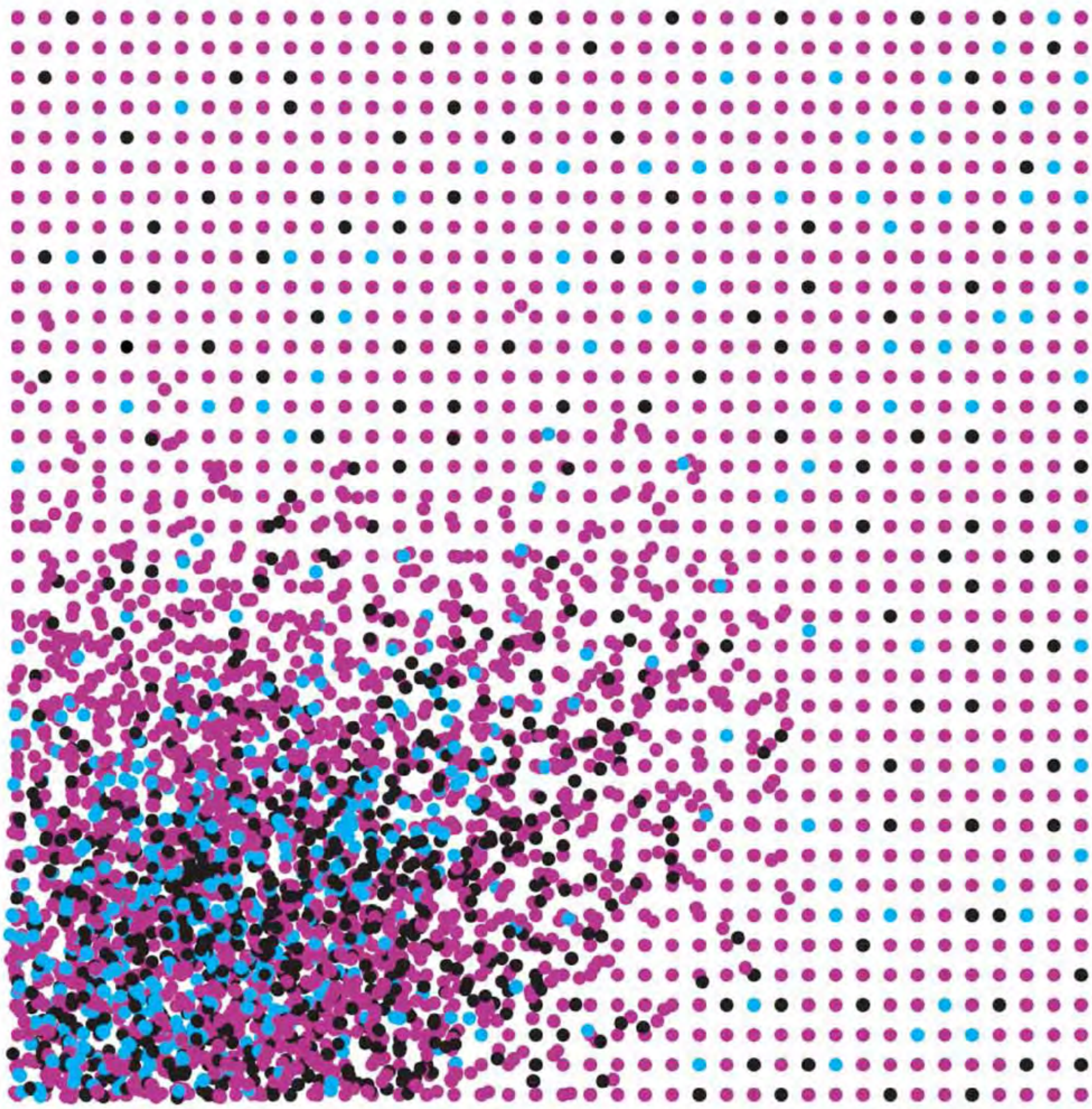
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MANAGING FORWARD

THE RESET ECONOMY *Getting ready for the post-recession world*

BY IAN ROWLEY



CEO Watanabe apologized for losses in March. Nomura shares are now up 79%

MICHAEL CARONNA/REUTERS

NOMURA IS STARTING TO FLEX ITS LEHMAN MUSCLES

When Japan's Nomura Holdings bought the European, Middle Eastern, and Asian operations of Lehman Brothers a year ago, the move seemed both inspired and reckless. Adding 8,000 Lehman employees tripled Nomura's size outside Japan, giving it the scale to reset its business model and boost its presence in key regions where it had been keen to expand.

Yet investors balked, sending Nomura's shares down by 70%. Their fears seemed to be confirmed this spring when Nomura said it was $7.5 billion in the red for the fiscal year ended in March. "This represents a record loss for Nomura and is something we are not proud of," CEO Kenichi Watanabe told investors.

Now, though, Watanabe's decision to plunk down $200 million-plus for Lehman's assets seems to be paying off. For the quarter ended in June, Nomura eked out earnings of $125 million, and brokerage NikkoCitigroup is now predicting a full-year profit, up from a previous estimate of a $560 million loss. Nomura's shares, meanwhile, have risen 79% from their March low.

There are signs that Lehmanites are bolstering Nomura's investment banking unit. In Europe, mining company Anglo American—which in June rejected a hostile bid—hired Nomura for advice on fending off takeover attempts. And Lehman recruits have teamed up with Nomura's Tokyo staff to advise Japanese drinkmaker Kirin on a $1.2 billion purchase of breweries from Philippines beer kingpin San Miguel—one of 19 Asian deals the firm has worked on outside Japan since January. Last year it did two.

Meanwhile, Nomura's bond and equities businesses have benefited from Lehman expertise. In July and August, Nomura traded more stocks on the London Stock Exchange than any other firm. Prior to the Lehman deal, Nomura ranked 82nd. Next up is a push into the U.S., where since January Nomura has boosted its head count by 40%, to 855. "Without the financial crisis, it would have been very difficult to visualize ourselves as a top-tier player," says Akira Maruyama, CEO of Nomura's global markets division.

Some Tokyo watchers think Nomura is well positioned to prosper even as rivals recover. "They got a very good price and they bought at a very good time," says Satish Betadpur, an analyst at Independent International Investment Research. The key will be hanging on to star bankers, though fears that ex-Lehman people could decamp this fall—when many are eligible for big bonuses—may be overblown. The Lehmanites are "great people who know the employment alternatives right now are not very good, so they'll stick around," says C.J. Wilson, founder of Global Alliance, a Tokyo investment firm.

Still, many wonder whether Nomura can emerge as a true rival to the likes of Goldman Sachs, Morgan Stanley, and UBS. One issue is merging a hard-charging New York investment bank with the more buttoned-down corporate culture of Tokyo. And some fret that even after a good start, Nomura could repeat past mistakes such as retaining too much control in Tokyo.

Insiders insist the Lehman deal put Nomura on the right track. The new hires, they say, will reinvigorate the bank's Japanese operation. One example: Nomura is now offering its Japanese staffers higher pay and bonuses in exchange for less job security. "We have a lot of work to do," Maruyama says, "but the new Nomura has been established." |BW|



HOW THE GLOBAL ECONOMY IS REBALANCING

This time Asia, the Americas, and Europe are all accelerating together. This synchronized rebound will lift trade broadly, to the benefit of U.S. exports

Looking back, it seems so clear: The wildly lopsided global economy was headed for trouble. By 2006 the U.S. trade deficit had ballooned to 6% of gross domestic product, a gap comparable to those of some Third World countries, except that the U.S. accounts for 21% of world GDP. Imports flooded ashore and dollars rushed abroad, greatly inflating trade surpluses overseas. In return, foreign currencies poured in, providing the capital America needed to finance its credit boom and devil-may-care consumption.

The worst U.S. recession since the 1930s has been a cruel way to rebalance the world economy, but it's working. Through the second quarter the trade deficit had fallen to 2.4% of GDP, and America had cut its need for foreign capital by 56%. Now comes the hard part: holding on to or maybe extending that progress as a U.S. and global recovery takes hold.

10.3%

Fall in trade-weighted value of the U.S. dollar, vs. a basket of currencies, since the 2009 high on Mar. 3

Data: Federal Reserve

The July trade report was good news for the near-term outlook, but it also suggested the road to rebalance will not be easy. A third consecutive monthly rise in exports showed the global recovery was gaining steam, and the second month of higher imports implied firmer U.S. demand. But the monthly deficit widened by $4.5 billion, the most in a year, to $32 billion, as a jump in imports overtook a strong gain in exports.

So, here we go again? Not necessarily. In the past, the trade deficit has typically widened sharply in a recovery, as the U.S. turned up in advance of other economies, causing imports to run ahead of exports. This time—with the global stimulus efforts kicking in and the financial markets healing—Asia, the Americas, and Europe are all accelerating together. A synchronized rebound will lift world trade broadly, much to the benefit of U.S. exports. At the same time the rebound in U.S. spending will be muted by tight credit and heavy consumer debt, limiting import growth and restraining the trade gap.

The global recovery is already starting to power U.S. exports. Shipments of goods, adjusted for inflation, rose at a 14% annual rate in the three months through July, after collapsing last autumn. Exports of industrial materials and capital goods, especially to emerging markets, account for the lion's share of the recent growth.

Export strength should broaden as developed economies—including Europe and Canada, which buy a third of U.S. exports—shift from recession to recovery. Economists say growth of key U.S. trading partners picked up to about a 4% annual rate last quarter, and they expect that pace to continue in the second half. The August index of export orders from the Institute for Supply Management surged to a level indicating further solid gains.

In addition to global growth, the dollar continues to do its part in the rebalancing act. The greenback's long-term decline, which makes U.S. goods more competitive, totaled 26% against all currencies from 2002 to 2008. That slide stopped temporarily last year as a flight to safety lifted the dollar, but the greenback is now retreating, and the decline should continue. The Federal Reserve's aim to keep U.S. interest rates exceptionally low compared with rates abroad makes dollar-denominated assets relatively less attractive.

One fear is that foreign investors will stop buying U.S. debt, just as Washington needs to borrow more. Such a turn could lead to a dollar collapse, causing spikes in long-term rates and inflation. But although Uncle Sam may be borrowing more, consumer credit has plunged, sharply reducing the U.S.'s need for foreign capital. The balance-of-payments deficit, which is essentially foreign lending to the U.S., shrank to $98.8 billion in the second quarter, from a peak of $214.8 billion nearly three years ago (chart).

The less the U.S. needs to borrow from abroad, the less downward pressure on the dollar—and the greater the balance in the global economy. Maintaining a better balance in the long run will be difficult, however. Export-intensive nations, such as China, must boost their domestic demand, and the U.S. must hold its hunger for imports in check while exporting more. Unfortunately, old habits die hard. | BW |

AMERICA'S REDUCED APPETITE FOR FOREIGN CAPITAL



Data: Bureau of Economic Analysis, IHS Global Insight

BRAD TRENT

NUMBERS

RECONSIDERING CONSUMERS' IMPACT ON THE U.S. ECONOMY

By Michael Mandel/Charts by David Foster

We often hear consumer spending is 70% of economic activity since "personal consumption expenditures" total $10 trillion out of $14 trillion in GDP. But this overstates the importance of consumers to the U.S. economy. PCE includes imported goods such as consumer electronics, which mainly stimulate foreign production. It also includes nonconsumer items, such as spending by religious groups. All told, household "out-of-pocket" spending drives roughly 40% of U.S. economic activity.

What it includes: Operating expenses of religious groups and other nonprofit institutions in excess of sales of goods and services.

Consequence: Most of this spending is controlled by nonprofit boards or government funders rather than households.

What it includes: Items like "rental of owner-occupied nonfarm housing"—what you theoretically pay yourself to live in your own home. Imputed services do not represent household cash outlays.

Consequence: Does not directly support U.S. economic activity.

What it includes: Clothes, electronics, motor vehicles and parts, gasoline, and other goods with significant import components.

Consequence: Supports both foreign and U.S. production.

What it includes: Almost all health-care outlays by consumers, employer health plans, and government programs like Medicare.

Consequence: Only about 15% of this category comes directly from households. Third-party providers control the rest.

What it includes: Everything from food to haircuts to legal fees—any consumer good or service produced mainly in the U.S.

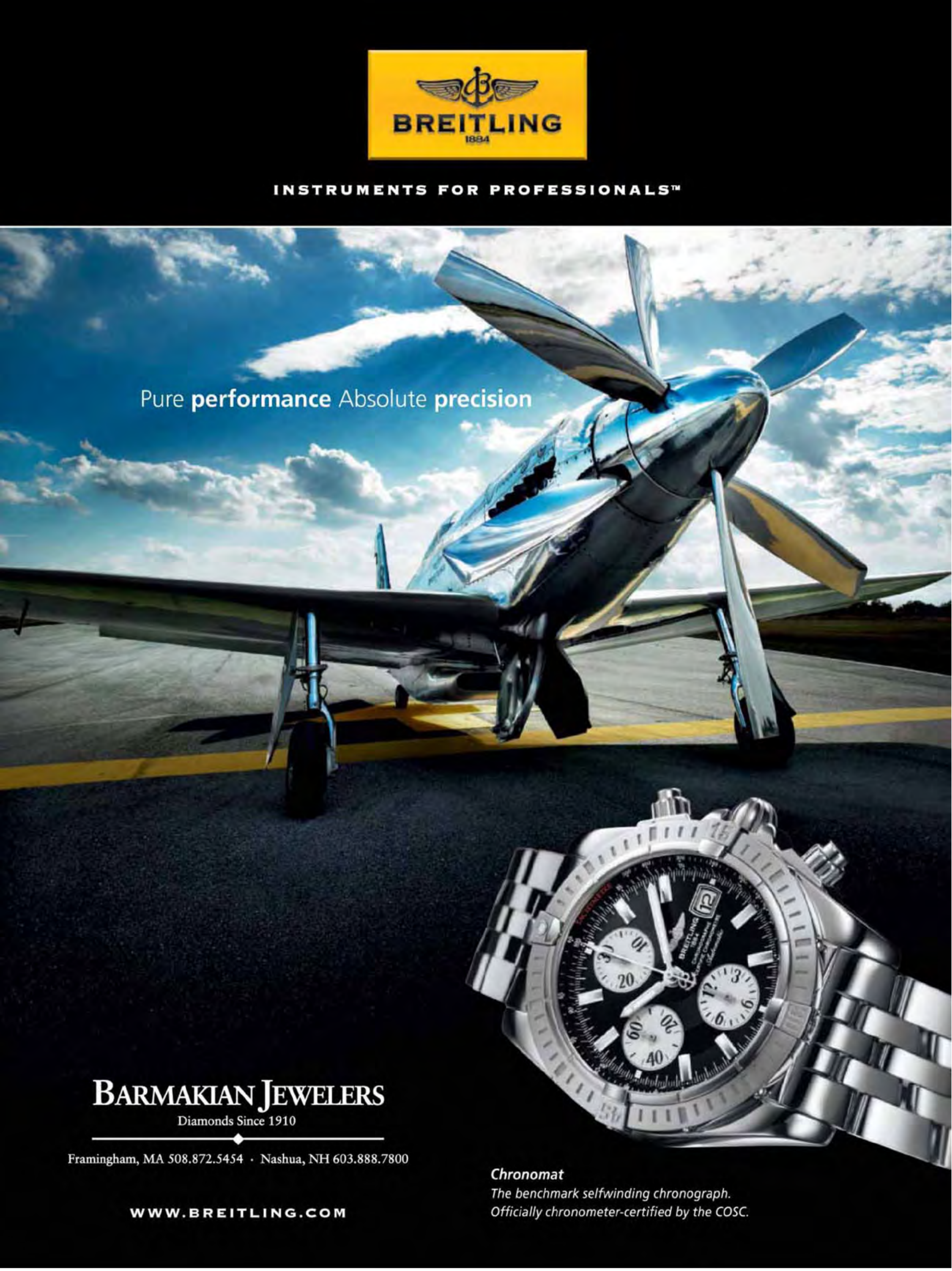
Consequence: Feeds directly into domestic economic activity.



NOTE: The direct impact of household spending on the U.S. economy is estimated as outlays on domestically produced goods and services, plus half of import-intensive goods, plus 15% of health-care goods and services

*Average of four quarters ending second quarter 2009
**Not elsewhere counted

Data: BEA, *BusinessWeek*


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EDITED BY DEBORAH STEAD



KID-FRIENDLY BOOK TOURS (AUTHOR NOT INCLUDED)

For years, publishing houses have flown authors around the country to promote their latest works. But with book sales down 3% last year, publishers, like marketers of all stripes, are trying to be more creative. Consider the authorless book tour. Ever since Random House launched its Stupid Smelly Bus Tour six years ago to promote Barbara Park's Junie B. Jones series for kids 4 to 8, the idea of leaving the author at home has gained momentum in children's publishing, a $3.3 billion slice of the $24 billion book industry. Without the writer, says Michael Norris, a senior analyst at Simba Information in Stamford, Conn., "There is a lot more a publisher can do." The tours focus instead on the books' characters (who engage kids more than authors do) and hit venues beyond big cities. To promote the just-published *Junie B.'s Essential Survival Guide to School*, this fall's 16-stop tour (with an actress as Junie) will hit modest Milford, N.H. Noreen Marchisi, publicity director for Random House children's books, says the bus promotion costs more than an author tour, but the sales it sparks justify the expense.

This summer, Amulet Books, an imprint of Abrams, did a 20-day Ice Cream Truck summer reading tour, dishing out free scoops at 31 city libraries to publicize the October 2009 launch of the fourth book in Jeff Kinney's Wimpy Kid series (ages 7 to 12), which has sold more than 20 million copies. "Preselling a book is more important than ever," says Abrams publicity and marketing director Jason Wells, who declined to say what the tour cost but noted that traditional readings take a chunk of authors' time when "we need them writing."

And on a recent September afternoon, about 30 children jammed into Manhattan's Books of Wonder to join actors in interactive skits based on John Flanagan's Ranger's Apprentice medieval fantasy series, published by Penguin Group's Philomel imprint (ages 10 and up). Don Weisberg, president of Penguin Young Readers Group, says the 26-stop tour costs Penguin 25% more than author readings. At the bookshop, Milton Cohen, 7, seemed to enjoy the show, pleading afterward with his grandmother to buy one of the Flanagan books. Would he rather have met the author? "Nah," he said.

–*Matthew Boyle*

ILLUSTRATION BY YAREK WASZUL



CAFE, CROISSANT, *ET* WINDOWS 7

Coming soon to France: a different kind of computer pop-up. Microsoft will open a temporary café in Paris on Oct. 22 to create buzz for the global launch of its Windows 7 operating system on that day. The planned Windows Café, near the busy Chatelet-Les Halles commuter rail station, will be a first for Microsoft. It's modeled after the pop-up stores—those that open without warning and close after a short time—used by retailers such as Gap and Nike to promote new products.

The Windows Café will sell espresso, latte, and snacks as customers test-drive Windows 7 and other software on PCs, mobile devices, and Xbox game consoles. But no software or hardware will be sold. "The café is just a temporary marketing scheme and will be open only for a few months," says Clémence Brondel, a publicist for Microsoft in France. Michael Cherry, an analyst at Directions on Microsoft, a Kirkland (Wash.) firm that tracks Microsoft, says the café shows the company's "shotgun" marketing approach, which lets subsidiaries worldwide run their own promos. Microsoft says it's not planning pop-ups elsewhere. But "if the café works," Cherry says (and he predicts it will), "I'm sure it will be replicated in another market." *–Leona Liu*

COLLEGE: RISING COSTS, DIMINISHING RETURNS

This hasn't been a good decade so far for young college grads. Full-time workers ages 25 to 34 with only bachelor's degrees saw a sharp 11% decline in their real earnings between the end of the tech boom in 2000 and 2008. That's according to income statistics released on Sept. 10 by the U.S. Census Bureau. The drop in pay for young college grads looks even worse when compared with the continuing rise in college costs over the same stretch (chart). Adjusted for inflation, tuition, fees, and room and board rose 23% at private four-year schools and 36% at public institutions. The final blow: Young college grads saw a bigger pay drop, on a percentage basis, than peers with only an associate degree. *–Michael Mandel*



College costs have climbed as pay for grads has dropped

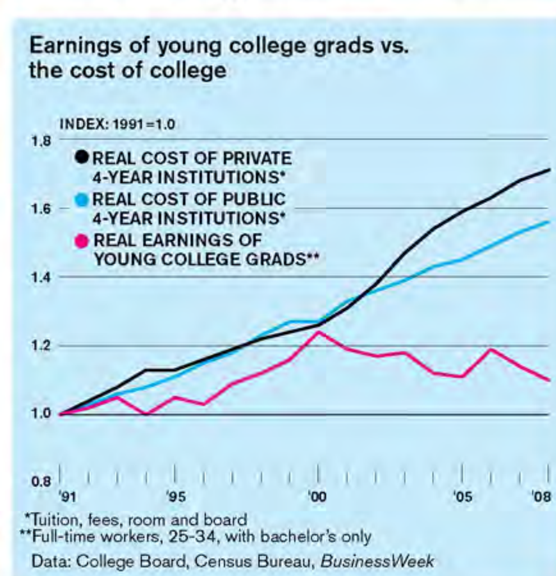


ILLUSTRATION BY GRACIA LAM; PHOTOGRAPH BY CHRISTOPHER CHURCHILL/RAPPORT; CHART BY LAUREL DAUNIS-ALLEN/BW


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FINANCIAL INNOVATION UNDER FIRE

Can we protect consumers and still be creative?

BRIAN STAUFFER

By Peter Coy

Leave it to Wall Street to give innovation a bad name. Americans prize out-of-the-box thinking in technology and culture, but they fear it in finance—understandably, thanks to innovative disasters like credit default swaps, collateralized debt obligations, and "negatively amortizing" mortgages whose principal grows instead of shrinking.

In spite of the public's mistrust, entrepreneurs and academics are plunging ahead. They're working on ideas they hope will help the consumer borrow more safely and build wealth more reliably. Some are ambitious, like reducing homeowners' exposure to declines in local housing prices. Others are fanciful, like an electronically rigged wallet that becomes harder to open when your bank account is low, an idea from the Massachusetts Institute of Technology.

The big problem: It's hard to tell the beneficial ideas

from the ones that are self-serving or dangerous. Many top economists, including former Federal Reserve Chairman Alan Greenspan, once lauded subprime mortgages as a fantastic innovation. With this fresh in mind, there's a risk that government will overreact and suppress good ideas along with bad ones.

The lightning rod for the debate over innovation is the Obama Administration's proposed Consumer Financial Protection Agency, which would vet new financial products for safety (page 26). Bankers and laissez-faire economists object that government is bad at picking winners and losers. Andrew W. Lo, director of the MIT Laboratory for Financial Engineering, who trained the geniuses responsible for some of the exotic derivatives that blew up, favors letting markets work: "Financial technology is no different from any other technology. It goes through a maturation process. Version 2.0 is going to be better than version 1.1."

Many free-market economists do acknowledge that some regulation is appropriate in the wake of the crisis. Lo, for example, favors both controls on new technologies with no redeeming social value and government-led safety testing of new financial technologies.

But some economists go further and argue that any financial innovation is guilty until proven innocent. Former International Monetary Fund chief economist Simon Johnson and James Kwak, authors of the popular Baseline Scenario blog, wrote in the summer issue of the journal *Democracy* that innovation often generates unproductive or even destructive transactions. "The presumption should be that innovation in financial products is costly ... and should have to justify itself against those costs," they wrote. The two bloggers support the Consumer Financial Protection Agency.

A more productive approach may be that of Yale University economist Robert J. Shiller, who sees a role for government in guiding innovation. The father of the Case-Shiller home price indexes sounded alarms about the bubbles in tech stocks and later in housing. Shiller favors the CFPA but worries about overkill. He says he was dismayed by the bureaucratic hurdles his company, MacroMarkets, faced before launching house-price derivatives this year on the New York Stock Exchange.



Yale's Shiller favors an agency to vet products but warns of regulatory hurdles

Regulation complicates even the rollout of financial products and services that are seemingly pro-consumer. For example, prepaid debit cards allow people who don't have checking accounts to make electronic payments and avoid carrying around a lot of cash. But they're controversial with regulators because the convenience comes at a cost: high fees. On the other hand, fee-cutting innovations have also encountered difficulties. The hot trend of peer-to-peer lending, which matches small-scale borrowers and lenders on the Web, gives borrowers a way of avoiding bank charges. Still, peer-to-peer companies like Prosper, Lending Club, and People Capital were nearly killed in 2008 by a ruling that the firms had to restructure their loans as securities and register with the Securities & Exchange Commission. They have managed to soldier on.

Assessing the usefulness of innovations can be difficult. Progress Financial in Mountain View, Calif., doing business in the state as Progreso Financiero, makes small, short-term loans to low-income Hispanic customers via desks in supermarkets and other convenient locations. California limits effective interest rates on such loans, factoring in fees, to around 36%. Sounds reasonable, but Progress Financial CEO James Gutierrez says the cap is stunting the growth of the sector, noting that firms like his are competing with payday lenders that can charge effective annualized rates of 400%.

Few people in either government or the private sector are thinking on the grand scale of President Franklin D. Roosevelt's brain trust in the Depression, which launched Social Security and federal deposit insurance. Yale's Shiller has encountered scant interest in some sweeping ideas he has for protecting consumers from needless risks. One is "home equity insurance"—a policy that would pay off if values of homes in your area fell (regardless of what happened to the value of your own house). Another is an income-linked mortgage: Your monthly payment would automatically adjust downward if salaries in your chosen profession fell (regardless of what happened to your own salary).

Shiller says the government should fund consumer-finance research and build indexes that could underlie new products like those income-linked mortgages. Shiller's ideas aren't the only ones out there, but giving government a role in nurturing financial innovation may be the best way forward. |BW|

REGULATING FINANCIAL INNOVATION: THREE VIEWS

Economists and policymakers are divided over the right way to regulate innovative consumer financial products. Here are the three main perspectives.

LAISSEZ-FAIRE

Mistakes were made with subprime mortgages, but the next generation of consumer financial innovations will be better. Too much regulation will crimp creativity and actually hurt consumers.

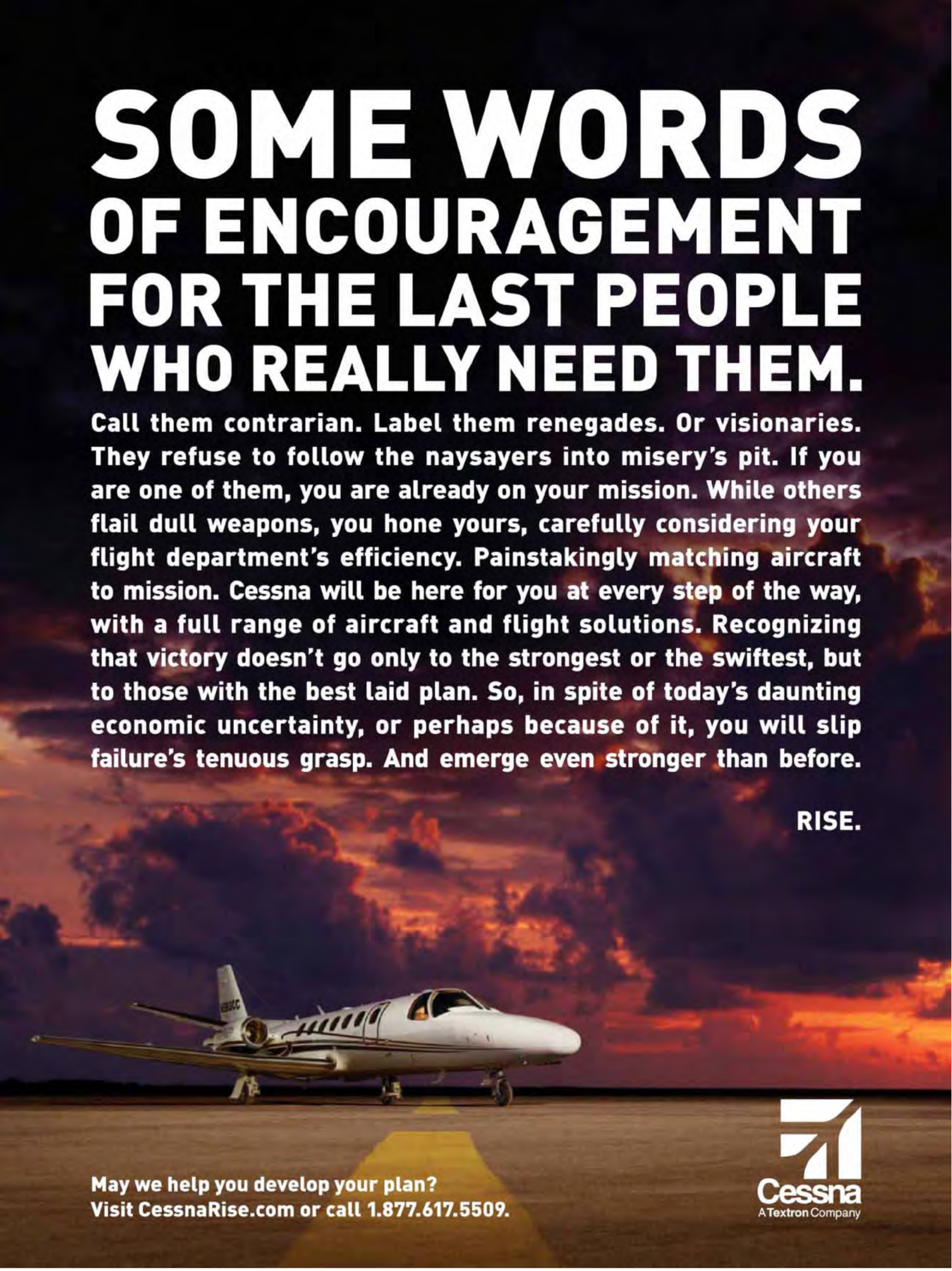
PRESUMED GUILTY

All too often financial innovations don't provide significant benefits to consumers. New products should be required to serve a real need, and consumers should be educated about the risks.

GUIDED INNOVATION

New ideas can be positive for consumers, but they can't be left solely to Wall Street. The government should identify areas needing improvement and encourage innovation with targeted R&D.

MICHAEL LEWIS/CORBIS OUTLINE


SOME WORDS OF ENCOURAGEMENT FOR THE LAST PEOPLE WHO REALLY NEED THEM.
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MAIN STREET VS. THE WHITE HOUSE

The financial industry and its allies are enlisting small business in the fight against a new federal watchdog

By Jane Sasseen

In his Sept. 14 speech on Wall Street, President Barack Obama argued that the financial crisis occurred in part because no single agency was in charge of blocking abusive lending to consumers. "That is what we'll change," he said. "The Consumer Financial Protection Agency will have the power to ensure that consumers get information that is clear and concise, and to prevent the worst kinds of abuses."

For a White House fighting the perception it has gone easy on big banks, winning Congress' approval for the Consumer Financial Protection Agency (CFPA) is a top priority. Yet the financial services industry, while agreeing more protection is needed, fears the agency would limit many lucrative products. So it has put killing the CFPA near the top of its to-do list. A key industry tactic is to refocus the debate around small business owners and the small community banks that serve them. "If they can convince Congress that this isn't about helping the little guy but about strangling the little businessman, then they've got a shot," says one financial services lobbyist who is not involved but is watching the fight closely.

The plan grew out of a June 24 meeting of financial services trade groups, the U.S. Chamber of Commerce, and other K Street allies at the D.C. offices of lobbyist Locke Lord Strategies. The group agreed its best chance was to raise doubts among business-friendly Democrats in Congress.

SMALL BANKERS BALK

By mid-July, a draft memo entitled "The CFPA: Five Reasons Why it Could Do More Harm than Good" began circulating. "Consumers will have fewer, less flexible options to meet their financial needs" reads one bullet point. "The federal government will be put in the role of deciding which financial products and services best fit the needs of consumers" reads another.

Since then hundreds of bankers have hit Capitol Hill, many arguing that CFPA's restrictions would limit innovation and raise the cost of credit. "I have a problem with removing ingenuity from the industry entirely," says Julieann M. Thurlow, head of Reading Co-operative Bank in Reading, Mass. She's joined conference calls with Assistant Treasury Secretary Michael Barr and other officials to voice her opposition to various aspects of the CFPA.

The Chamber of Commerce is also claiming that all small businesses that offer credit, not to mention their accountants and ad agencies, could find themselves in the agency's ever-tighter grip. "This bill is not about protecting consumers," says Tom Quaadman, a Chamber point man on finance. "It is about increasing big government." Thanks to the Chamber's campaign, by Labor Day, 17,000 anti-CFPA letters had reached Congress.

Those Democrats working on the bill say these arguments bear little relation to reality. One Treasury official says any unintended effect on small businesses is readily fixable. "No one is trying to keep shopkeepers from extending credit," adds Obama's chief economic adviser, Larry Summers.

True or not, the claims are having an impact. The House Financial Services Committee was to begin moving the bill in July. Now, October appears to be the earliest date. Some Democrats are voicing doubts. After Obama's speech, Paul E. Kanjorski (D-Pa.), a key member of the House committee, asked if a separate agency were really needed.

Howard Glaser, ex-chief lobbyist for the Mortgage Bankers Assn. who now runs his own firm, argues that without big revisions the bill won't pass. "Until now the message has been more controlled by the opponents than the Administration," he says. Time is running out for the White House. |BW|

–With Theo Francis in Washington



BRIAN STAUFFER



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028

USDA HOME LOANS: SUBPRIME REDUX?

Builders are jumping on a no-money-down program to bolster sales in depressed markets. Sounds familiar

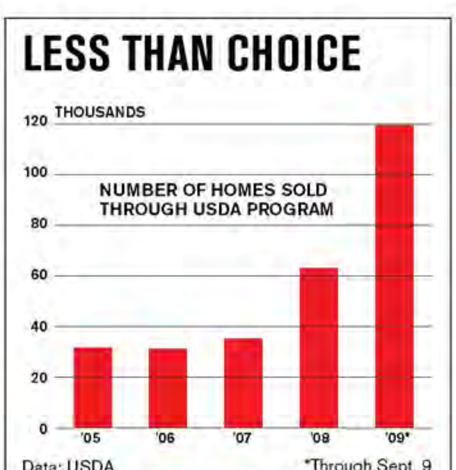


By Mara Der Hovanesian

Builders and lenders are dusting off a familiar pitch: mortgages with $0 down and 100% financing. The deals, which take advantage of a little-known loan program at the U.S. Agriculture Dept., are bolstering sales in some areas. These new mortgages share some characteristics with the old ones now wreaking havoc on the housing market—and critics fear lending standards could slip. Says Daniel Oppenheimer, an analyst with Credit Suisse: "Unlike beef, these loans should be described as USDA subprime."

In the grand scheme of the $1.89 trillion residential real estate market, the USDA program—founded in 1949 to spur home sales and development in rural areas—is still a blip. But since the financial crisis, the program has exploded in size. As part of the Obama Administration's effort to prop up housing, the U.S. allocated $10.5 billion to the Agriculture Dept.'s guaranteed loan program this year, up from $6 billion in 2008 and $3 billion in the past.

The result: The number of home loans guaranteed by the USDA swelled to nearly 120,000 in the first nine months of 2009, up from roughly 35,000 in all of 2007. Given the rampant development during the boom, many communities where the USDA loans are available aren't technically "rural" anymore—and include exurbs near big cities. Ashley-Gayle Boothe and her husband Scott have applied for a USDA-backed loan to buy their first home, a three-bedroom house 30 minutes north of Tampa, for $127,500. "We didn't want to put anything down," says Ashley-Gayle Boothe. "We figured we'd have to buy appliances."



Data: USDA

*Through Sept. 9

The government-backed loan program is buoying builders and lenders. Analysts say federal loans, including those guaranteed by the USDA, accounted for 64% of sales at builder D.R. Horton in the latest quarter. In Port St. Lucie, Fla.—a coastal town littered with foreclosures and empty subdivisions—roughly one in five mortgages is coming through the Agriculture Dept., according to local industry players. "Everyone is fighting for every little sale they can get, and the USDA financing is a huge opportunity," says Jim Belfiore, president of Belfiore Real Estate Consulting in Phoenix.

Housing experts question the wisdom of 100% financing for any borrower. Similar questionable lending decisions during the housing boom lie at the root of many distressed properties today. In the current environment the mortgages are particularly problematic since prices continue to fall in the areas where the Agriculture Dept. loans have proliferated. In one such place, Menifee, Calif., record foreclosures continue to depress home values. For owners, falling prices and no equity in their homes have proven a toxic combination, especially when they try to sell.

The USDA, builders, and lenders defend their use of the loans. The agency argues it adheres to strict underwriting standards, assessing each borrower's credit, income, and cash flow. Joaquin Tremlos, acting director of the USDA's home loan program, says the agency's portfolio of loans has a low default and delinquency rate. The USDA "has not relaxed our guidelines.... We've intensified them to make sure that these loans continue to be sound."

Even so, some observers worry the department will stumble under the flood of new loans. A similar program run by the Federal Housing Administration has experienced a significant uptick in fraud since the agency's share of the market ballooned this year. "Some people have cleverly figured out this [USDA program] is the way to target a good chunk of people," says Michael R. Widner, an analyst at Stifel Nicolaus Equity Research. "The question is, do they have the capacity to handle it? If you are getting massive growth, you are probably getting a good number of the wrong people." |BW|

ILLUSTRATION BY THOMAS FUCHS; CHART BY JOE RHAMES/BW


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A SECOND OPINION ON MALPRACTICE

For all the doctors' complaints, most studies suggest reforms won't have a huge effect on health-care costs

By Catherine Arnst

President Barack Obama tapped into a large vein of public support when he suggested recently that he is open to reforming medical malpractice laws. It's common currency in the U.S. that litigation drives medical inflation by forcing doctors and hospitals to resort to "defensive medicine," overtreating patients to avoid lawsuits.

The evidence suggests a much smaller effect. Study after study shows that costs associated with malpractice lawsuits make up 1% to 2% of the nation's $2.5 trillion annual health-care bill and that tort reform would barely make a dent in the total.

A comprehensive new report from Northwestern's Kellogg School of Management, using a database of employer-sponsored health plans covering 10 million Americans, looked at the impact of tort reform measures already enacted in more than 30 states. The authors concluded that comprehensive, nationwide reforms would lower overall health-care costs by 2.3% at most. "That's significant, of course, but still fairly small," says Kellogg professor Leemore S. Dafny, a co-author of the study. As President Obama told a joint session of Congress on Sept. 9: "I don't believe malpractice reform is a silver bullet."

Doctors see things differently. They pay malpractice premiums that can run up to $250,000 a year for specialties such as neurology or obstetrics. It's "a huge issue for us," says Dr. Steven M. Safyer, CEO of Montefiore Medical Center in New York. "I would say about 5% of our costs are directly attributable to malpractice premiums and another 5% to defensive medicine."

2.3%

Estimated reduction in overall health-care costs if significant medical malpractice reform is enacted

Data: Northwestern's Kellogg School of Management

A 2004 study by the Congressional Budget Office came up with much lower figures, however. The CBO estimated that malpractice premiums and awards to patients represent less than 2% of overall health-care spending. The CBO also concluded that any reductions in medical overtreatment from tort reform would be negligible. "So-called defensive medicine may be motivated less by liability concerns than by the income it generates for physicians," the government economists concluded.

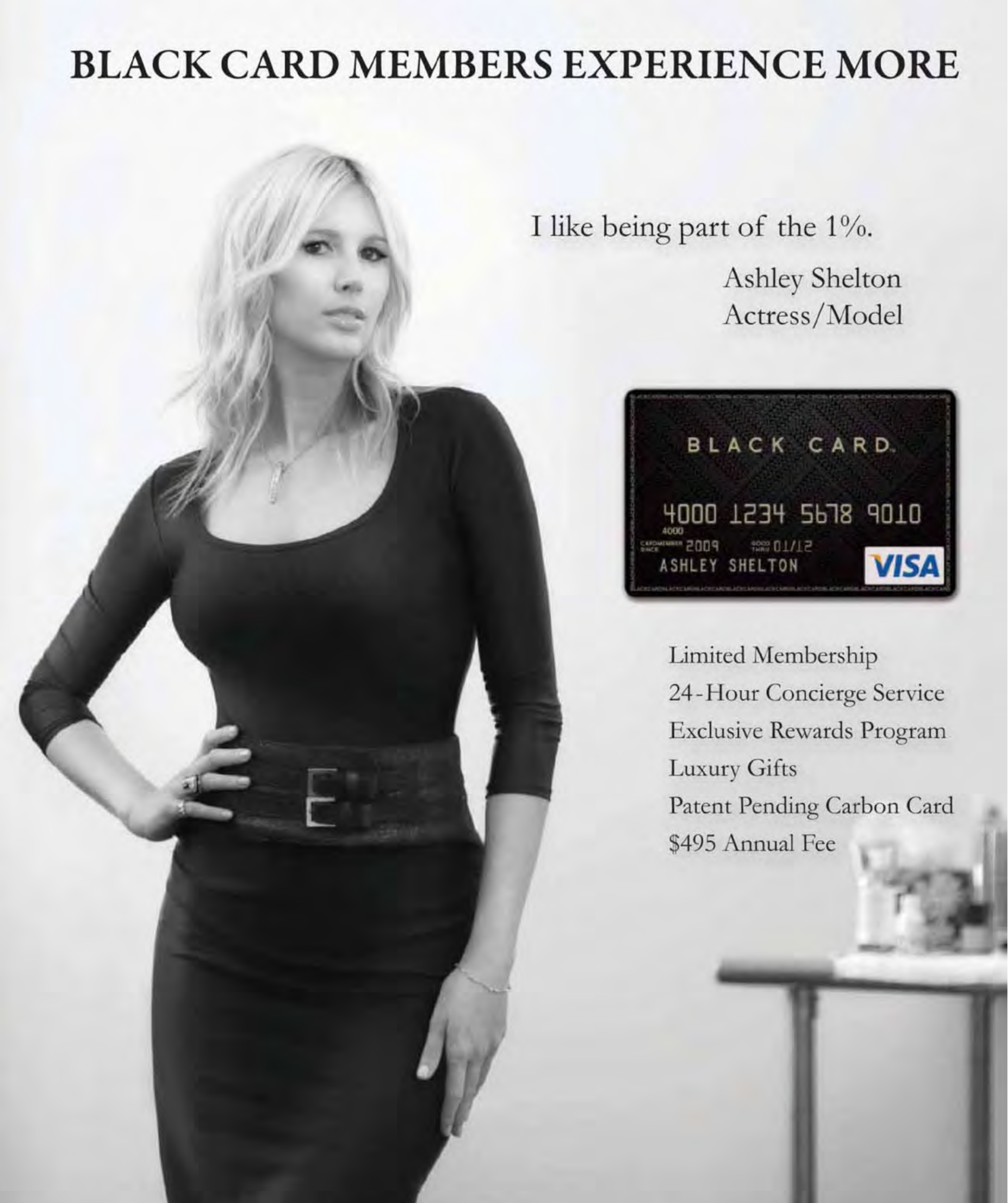
Malpractice lawsuits make up 1%-2% of the U.S. health-care bill, studies show

FAIR TO PATIENTS?

That makes sense, says Kellogg's Dafny: "We have some expectations about medical care that make it difficult to roll back the services that have always been delivered." Most doctors are paid by the number of services they provide. Since insured patients rarely pay the cost of additional treatments or tests, there is little pressure on doctors to scale back, even when the fear of being sued is removed.

Look at Texas, which enacted some of the most extensive malpractice reforms in the nation in 2003. The number of lawsuits in the state has fallen by half since then, and malpractice premiums are down 30%. But health-care costs in Texas are still among the highest in the nation and are growing at a faster rate than in most other states. "I think tort reform is a good idea as a carrot to get doctors to go along with more significant health-care reforms," says law professor Charles M. Silver of the University of Texas at Austin. "But as we've proved, it isn't the answer on its own."

Whether tort reform is fair to patients is another point of contention. The Institute of Medicine, an independent adviser to the government, estimates that as many as 100,000 Americans die yearly from medical mistakes. But only about 4% of injured patients or their families sue, according to a Harvard study. And only 1 in 5 lawsuits awards the patient. "The amazing thing is that more patients don't sue," says Paul H. Keckley, director of Deloitte's Center for Health Solutions. |BW|



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NEW STEEL IN PITTSBURGH

Medical center UPMC has helped make the G-20 meeting's host city a model for Rust Belt revival

By Steve Hamm

When leaders of the world's powerful nations gather in Pittsburgh on Sept. 24 for the G-20 meetings, they'll doubtless spot the 20-foot-tall letters on top of the rust-stained U.S. Steel Tower spelling out "UPMC"—for University of Pittsburgh Medical Center. But they might miss the underlying symbolism: Health care and higher education have replaced steel as the city's economic engine.

$2 billion

Annual economic impact of biomedical research in Pittsburgh.

Data: Tripp Umbach

Pittsburgh was devastated by the loss of 100,000 manufacturing jobs in the 1980s. But what locals fondly call "eds and meds" have helped stabilize the city of 313,000. Now they're trying to build on that to make the city a center of high-tech innovation. Although the city still faces an uphill battle, it is hailed as a beacon for communities that seem to have been left behind by history. That's why the Obama Administration chose it to host the G-20. "Pittsburgh stands as a bold example of how to create new jobs and industries while transitioning to a 21st century economy," the President said on Sept. 8.

At the heart of the revitalization is UPMC. The nonprofit health-care giant, with an annual budget of $8 billion, operates 20 hospitals and employs 50,000 people. Along with the University of Pittsburgh and Carnegie Mellon University, UPMC has made local economic development one of its priorities. "The cities of the future, of which Pittsburgh will be one, will be driven by companies like UPMC and sophisticated universities that take intellectual property and translate it into services and commerce," predicts Jeffrey A. Romoff, chief executive of UPMC.

The jobs lost in heavy industry have been more than made up for by new ones created in health care, software, and green technologies.

Still, job growth is slow even in good times. The problem: The city has not yet produced a critical mass of high-tech startups that can grow to be major employers. To remedy that situation, UPMC in 2005 set up a commercial arm that has invested about $130 million in 20 medical technology, healthcare, and biotech companies—and partnerships with the likes of General Electric and IBM. UPMC's newest brainstorm is to set up a vaccine factory using cutting-edge technology it claims will slash in half the time and money it takes to set up a manufacturing plant. The potential payoff for the local economy: 6,000 construction jobs and 1,000 permanent positions.



CEO Romoff says cities of the future will be driven by companies like UPMC

MICHAEL NEMETH/WONDERFUL MACHINE

UPMC is also determined to be a leader in the digitization of medical records. With that goal in mind, it joined with others to invest $35 million in dbMotion, an Israeli-based startup whose software melds medical data from disparate sources. DbMotion set up its U.S. headquarters in Pittsburgh, and in the past year boosted its staff there from 3 to 25. "The UPMC partnership put us on the map and gives us a place where we can test out our technology with a leading-edge partner," says Peter A. McClennen, president of dbMotion's North American operations.

Pittsburgh offers lessons for other communities. Its leaders didn't spend a lot of energy trying to save troubled steel companies, suggesting it may be more valuable to look at new opportunities than old standbys. The city's experience also shows that persistence with new ventures is critical. "Pittsburgh people take the long view," says Paul O. Umbach, president and CEO of strategy consultant Tripp Umbach. "They do economic development the way the Steelers play football. Not flashy. You win as a team. You get the job done." |BW|

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APPS TRUMP TUNES AT APPLE

Music is less crucial as iPod sales ease and the company focuses on software



GLUEKIT

By Peter Burrows

Right after unveiling new iPods and iTunes software at an event on Sept. 9, Apple Chief Executive Steve Jobs invited singer Norah Jones on stage to perform for the assembled tech and media pundits. "Like you, we love music," he told the crowd. "That's probably the primary reason we do this."

The music industry had better hope Jobs & Co. keeps that passion because, from a business point of view, music isn't nearly as important to Apple as it once was. While Apple built its comeback over the past decade on its music-playing iPods, sales of those devices are expected to be flat in the years ahead.

So Apple is shifting its focus to new kinds of content. The Sept. 9 event was billed as a music-oriented affair, but Jobs spent much of the time showing off the game-playing abilities of the iPod Touch and new camcorder features in the iPod nano. Analysts say the most critical driver of Apple sales in the future will be the thousands of software programs, or "apps," that owners of iPhones and iPod Touches can download from the company's online App Store. "It's no contest," says Needham analyst Charles Wolf. "Apple's strategic future is tied to the App Store. There is no strategic importance to music anymore."

That leaves the music industry in a precarious spot, since Apple plays a more important role in their business than ever before. It is the world's largest music distributor, having passed Wal-Mart Stores in early 2008. Apple sells around 90% of song downloads and 75% of digital music players in the U.S. Since so few people are interested in listening to music on non-Apple products, digital music schemes that aren't blessed by Apple typically die young. The upshot: While the record labels need to crank up digital sales to counter falling CD sales, they're dependent on a company that's becoming less dependent on them.

The record labels depend on Apple, but the company is increasingly turning to a broad variety of applications for its future profits

Apple executives insist music is still central to the company's mission. IPhone owners want music along with those other apps, and digital downloads are growing fast. Apple says it has ratcheted up the number of employees on its music team over the past two years. Apple is also providing more room for others to innovate as it broadens its focus. For example, the company long took a dim view of outfits that tried to develop iPhone apps that competed with Apple's services. But on Sept. 10 the company quickly approved an application by Real Networks' Rhapsody, which sells music subscriptions as well as songs for download. "We sailed right through," says Rhapsody Vice-President Neil Smith.

The question is whether other companies can come up with the record-selling innovations the major labels once looked to Apple to create. There are some successes. An application from startup Pandora for personalized radio stations is downloaded about 20,000 times each day from iTunes, says Tim Westergren, Pandora's chief strategy officer. The company's popularity helps the labels two ways: Pandora pays the labels for any music played on its service (unlike regular radio stations), and Pandora's internal surveys show that 45% of people who use Pandora buy more music, while only 1% buy less.

These are intriguing innovations, record label executives say. But none of the apps will be as important to music sales as iTunes itself, and some experts worry Apple isn't doing enough to improve the core service. Though the latest version of iTunes has new features, including a simpler approach to sharing songs, there's "nothing groundbreaking," says Ted Cohen, a former EMI executive and now managing director at consultant TAG Strategic.

Music executives are beginning to recognize that Apple's attentions are shifting. "Our biggest concern would be if they started resting on their laurels [in music]," says one senior executive at a major label. "We need them to continue innovating." |BW|

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THE OIL CRISIS SLAMMING MEXICO

Falling Pemex revenues are widening the budget gap, but the country can't boost output fast enough



ANDRE PENNER/AP PHOTO

By Geri Smith



MEXICO CITY

It's crunch time in Mexico. After years of surpluses, the country is facing a growing budget gap. The shortfall is sparking vigorous debate on shutting ministries, laying off federal workers, and raising taxes on soft drinks, phone service, and more. But the most pressing question—and one that Mexico's leaders seem unable to address—is how to reduce the Treasury's dependence on dwindling oil revenues.

State-owned Petróleos Mexicanos, or Pemex, contributes some 40% of the national budget. Problem is, output at its main offshore field is plummeting. Last year, Mexico produced some 2.6 million barrels of oil daily, down 30% from its 2004 peak; now, it's 2.5 million a day, and without major new discoveries, Mexico's reserves will last for just nine more years.

Pemex engineers have long known that production would fall, but politicians have failed to take the decline seriously—until now. In a speech to a jam-packed Congress on Sept. 15, Finance Secretary Agustín Carstens acknowledged that Mexico was in rough shape. In 2010 Pemex's contribution to the federal budget will fall by $15 billion—about what the country spends in four years on police, security, and the judicial branch, Carstens said. "No other nation has faced such a rapid, serious drop in revenues," he said.

To get Mexico on a more solid footing, the government is proposing $16.2 billion in spending cuts next year. Carstens promised to ax 10,000 high-level government jobs. And President Felipe Calderón's budget for next year would eliminate three min-





Calderón is proposing $16.2 billion in spending cuts next year

istries, including one overseeing the important tourism industry. Calderón's budget also includes a $13.1 billion increase in personal, corporate, and consumption taxes.

That has the opposition-controlled congress hopping mad. With the economy expected to contract by 7.7% this year, opposition politicians say higher taxes are something Mexico can ill afford. "If we want any chance of emerging from this slump, we must take on long-term debt and allow a bigger deficit," says David Penchyna, a ranking member of the center-left Institutional Revolutionary Party (PRI).

Mexico is already taking on more debt. This year it's headed toward a fiscal deficit that equals 2.3% of gross domestic product, vs. 0.1% in 2008. The deficit is expected to rise to 2.5% of GDP next year, or 3.1% when off-balance-sheet obligations such as a 14-year-old bank bailout are included, economists say.

POSSIBLE DOWNGRADES

While the gap may seem modest in comparison to Washington's 11% deficit, investors don't like the idea of more debt. Two agencies—Fitch Ratings and Standard & Poor's—have signaled a possible downgrade in Mexico's sovereign bond rating, though that likely wouldn't threaten the investment grade the country has enjoyed since 2000. "There is limited fiscal room for maneuvering in Mexico," says Lisa Schineller, an analyst at S&P. "We see a very challenging scenario over the coming years."

$35 billion

Pemex revenues for the first half of 2009, vs. $52 billion for the same period in 2008

Data: Pemex

And don't expect Pemex to bail out Mexico City anytime soon. Because its main oil field, called Cantarell, was one of the world's most productive for decades after its discovery in the 1970s, the politicians who controlled Pemex's budget scrimped on spending for exploration. As crude exports have plummeted, these officials have started to understand that Pemex needs greater support. Since 2004 the government has nearly doubled investment in Pemex, to more than $20 billion this year. But it will take time for that to make up for declining output at Cantarell, which means the government needs to find new sources of revenue—fast. "You can't just discover and start producing more oil overnight. It can take years," says Jonathan Heath, chief Latin America economist for HSBC bank. "We're facing a permanent problem that other countries don't have." |BW|



100 BEST GLOBAL BRANDS

THE GREAT TRUST OFFENSIVE

By David Kiley
and Burt Helm
Photograph
by Michael L. Abramson

Companies as diverse as McDonald's, Ford, and American Express are revamping their marketing to win back that most valuable of corporate assets

"The spark began where it always begins, at a restaurant downtown, in a shop on Main Street," intones a narrator as the camera lingers in a restaurant, bakery, and bike factory. "Entrepreneurs like these are the most powerful force in the economy. As we look to the future, they'll be there ahead of us." The music swells, and the narrator concludes: "While we're sure we don't know all the answers, we do know one thing for certain. We want to help."

The commercial, which began airing across the U.S. this summer, was developed by Ogilvy & Mather for American Express. Its mission: to cast AmEx not as a financial titan but as a humble service provider assisting mom and pops—establishments consumers typically like to support. AmEx, its gold-plated reputation tarnished by subprime bets, wants to regain the trust of its customers.

In the world of branding, trust is the most perishable of assets. Polling in recent months shows that increasing numbers of consumers distrust not just the obvious suspects—the banks—but business as a whole. In a phone survey conducted from May 26 to July 3 by public relations firm Edelman, only 44% of Americans said they trusted business, down from 58% in the fall of 2007. The shift in sentiment is forcing companies from Ford Motor to AmEx to tweak marketing and focus on rebuilding credibility. "Trust is what drives profit margin and share price," says Larry Light, CEO of the Stamford (Conn.) brand consultancy Arcature and a veteran of McDonald's and ad agencies BBDO Worldwide and Bates Worldwide. "It is what consumers are looking for and what they share with one another."

Not long ago, trust and reputation were the domain of the PR department. Marketing executives, by contrast, pushed products and brands using the classic Procter & Gamble two-step: spending huge sums to maintain "share of voice"—marketing speak for outspending rivals to drive brand awareness—and endlessly reminding consumers of the "unique selling proposition" (Tide won't fade colors).

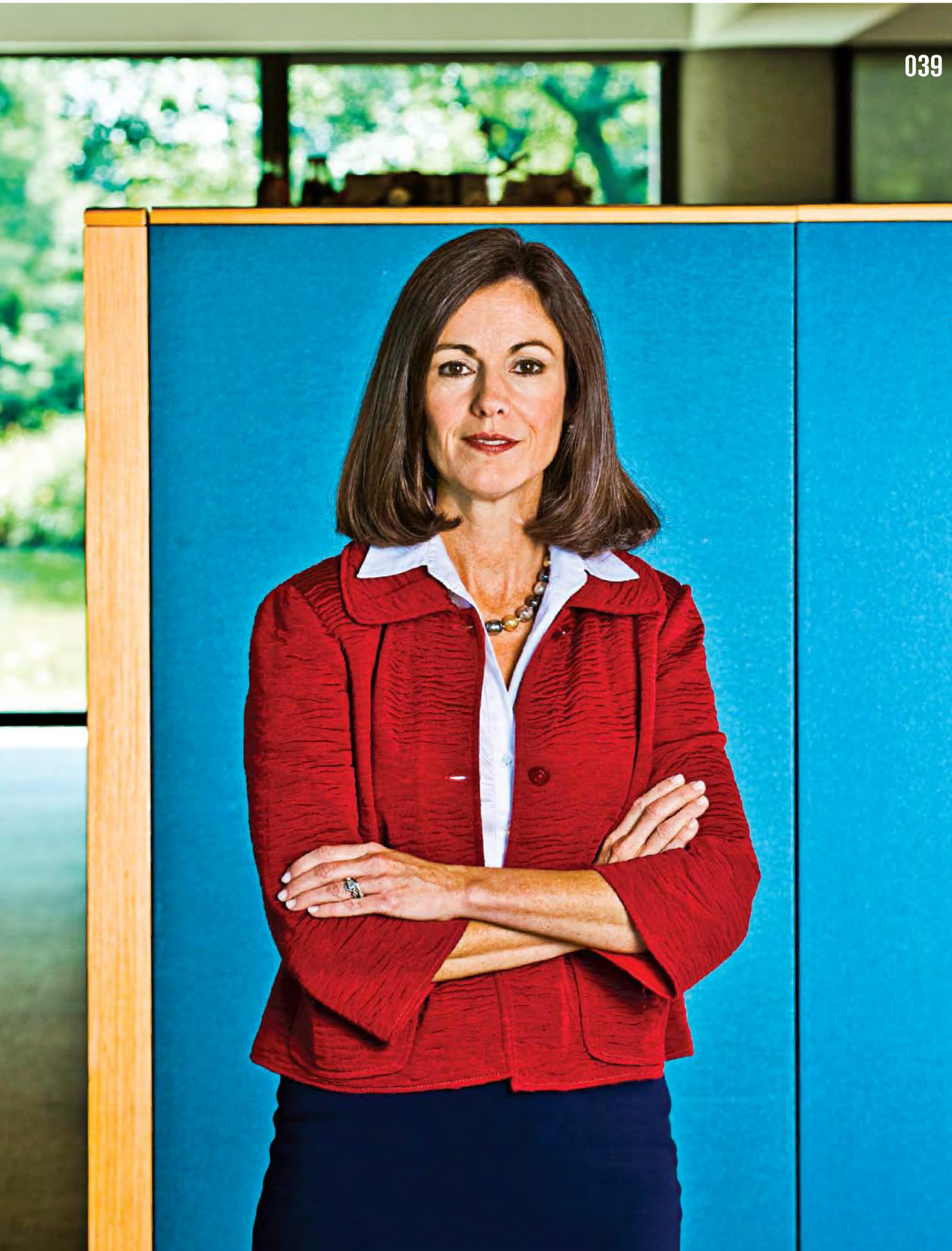
A NEW DAY

That approach doesn't work so well now—and not just because recession, job insecurity, and hammered home values have made consumers disinclined to part with their coin. The days of consumers passively absorbing a TV commercial—or, for that matter, a banner ad—are over. People research purchases as never before, and they read peers' opinions about brands and products. Meanwhile, the Web and smartphone have given companies a cheap way to reach consumers and adjust their message on the fly. That, says Light, is why "share of voice and unique selling propositions are easily copied by competitors."

Even before the economic meltdown, companies with trust issues began real-



McDonald's Dillon says trust and transparency are more important than ever



izing they couldn't keep talking past the problem with slick television commercials. One of those companies was McDonald's, long vilified for serving unhealthy food. Global Chief Marketing Officer Mary Dillon says McDonald's made a tactical decision to enter the conversation. "Trust and transparency [are] more important to us than ever," she says.

After years of fending off—or ignoring—critics, McDonald's has begun working with them. Following pressure from the People for the Ethical Treatment of Animals, McDonald's used its influence to force egg suppliers to raise the living standards of hens and cease debeaking them. PETA has publicly lauded the company for its efforts. The company declined to fight New York City's law forcing restaurants to post calorie counts on menus and says it supports making the rule national. Of course, McDonald's hasn't completely won over its critics. It is currently at an impasse with PETA, which wants U.S. poultry suppliers to stop using an electric jolt to kill chickens.

The fast-food giant, aware that many consumers still consider its food junk, talks constantly about the quality of its products, slicing off a chunk of its ad budget to focus on how it sources food. "We use 100% beef in every burger, and there's no percent better than that," reads one ad. The company's "Food, Nutrition & Fitness" Web site invites visitors to "meet" and "go behind the scenes with" the chain's beef, vegetable, chicken, and egg suppliers.

It's true that McDonald's cheap eats have helped it prosper during the recession and boosted the value of its brand. But its overall image appears to have improved, too. According to the global consulting firm Reputation Institute, McDonald's score, on a scale of 100, has climbed eight points since 2007, one of the fastest gainers, though its 63 remains slightly below average for all companies.

Auto brand stewards typically spend most of their money pushing new models. Ford Motor marketing chief Jim Farley is doing that. But he is also trying to build credibility by telling the world at large how well-managed Ford is (the implicit message being that Ford is better run than GM and Chrysler, which took taxpayer money to survive). Most car buyers are small business owners or employees, Farley notes, and have strong opinions about how companies are managed. "They will trust a company they believe is run really well," he says.

Ford has diverted money usually spent on vehicle discounts and used it to pump up the PR budget. A staffer, assigned to social networking full-time, generates a firehose of messages about Ford. These include the usual superlatives about the vehicles: their quality, style, fuel economy, and so forth. But the automaker's better-than-expected earnings have also been getting a relentless airing via Facebook, Twitter feeds, and sundry blogs. Communications staffers, meanwhile, are mining the company for stories that reflect how the company is being run more intelligently than its rivals—including its push to save costs by making one car for multiple markets. "Maintaining our independence from government ownership was a huge point of pride and fed into our guiding idea of a professionally run company," says Farley.

CONSUMERS ARE TELLING COMPANIES: "IF YOU AREN'T OPEN WITH ME, I WON'T TRUST YOU." IT'S COUNTERPRODUCTIVE TO FIGHT THAT

Ford's current ads, meanwhile, look nothing like previous campaigns. Gone are the warm, fuzzy, and inspirational commercials celebrating the American dream and hard work. The company no longer mines its 105-year history the way it used to, when it featured Chairman Bill Ford talking about innovation against archival footage of Model Ts and Henry Ford. Instead, the automaker is targeting consumers' rational left brain, relentlessly pushing themes that inspire street cred: new technology, fuel economy, quality scores. Farley says he has had to stare down colleagues and dealers complaining that the advertising is insufficiently uplifting. But he insists the new approach is working. Ford's retail market share is up 1 percent-

SERIOUS TRUST ISSUES



*Based on an annual survey of 400 "informed" Americans aged 35 to 64 published each January.
Data: Edelman

**Results of an interim survey conducted in June

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Ford's Farley says surviving the downturn without a bailout will be good for the brand

age point this year. Meanwhile, Ford is now spending $1,800 less on incentives per car than it did a year ago, and consumers are forking over on average $1,300 more for Ford models—a combination that drives the leading booster of customer trust: resale value.

Ford has a pretty good story to tell. Financial firms don't. And sometimes the first instinct is to duck. Randall Beard, who until recently was chief marketing officer at UBS's private wealth management group, recalls sitting at a strategy session last December when a senior executive said: "Our first strategy should be to try and stay out of the headlines." It didn't take a PhD in communications to know that wouldn't fly. Instead, Beard says, he tried to persuade the bank to be more transparent and open. Consumers are telling companies "in a thousand ways," says Beard, "that if you aren't open with me, then I won't trust you." It gets to be counterproductive to fight that, says Beard, who has since left the company, because "it's really easy for consumers to check and verify a company's behavior to find out if a company's actions match its words." UBS says it has armed staff with answers to potential queries from clients and set up a section on its Web site dedicated to explaining the U.S. Justice Dept.'s tax investigation into the company.

AmEx, as a consumer brand, had little choice but to rebuild its relationship with customers. The card issuer, which traditionally has targeted a more affluent demographic, has long had an image advantage over rivals Visa and MasterCard. That reputation was dented when it became clear that AmEx, like everybody else, had issued cards to risky borrowers.

Chief Marketing Officer John D. Hayes invited sales executives from three groups—consumer, small business, and the merchant services, which collects transaction fees when cards are swiped—to brainstorm a campaign about trust and caring that would reach all of their customers at once. The insight: Many of AmEx's merchant clients were small businesses. And average cardholders feel good about patronizing small businesses. That led to the television campaign.

At the end of the commercials, viewers are invited to visit Openforum.com, an AmEx Web site that provides tips for small businesses. AmEx is also cosponsoring NBC Universal's "Shine a Light," a contest in which people send in stories about their favorite neighborhood business. The winning business gets $100,000 in marketing support. AmEx spokesperson Ellen DeGeneres promoted it and twittered about it, reaching her 3 million-plus followers. "There are a lot of people concerned about what's happening to these storefronts," says Hayes. "We're not only saying we serve those people, it's demonstrating we've got their best interest in mind."

Will the trust offensive work? Image counselors caution executives to stay relevant to the current mood or risk being seen as spin merchants. "The AmEx ads should resonate because merchants, especially during a recession, want some form of acknowledgement that they are the economy's engine, not cultural villains," says crisis management consultant Eric Dezenhall. But he warns: "Trust-related marketing only works if there is a message that people want to believe in. You cannot spin an audience that doesn't want to be spun." |BW|

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Shifting Priorities

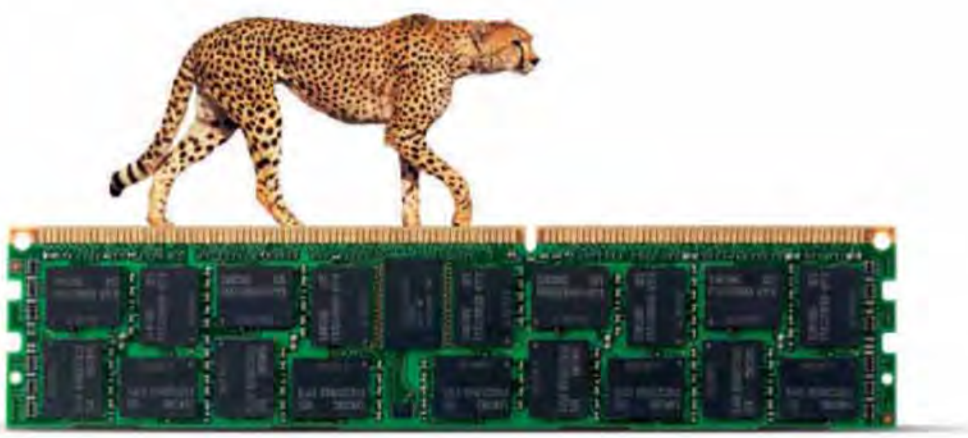
In Reputation Institute's latest Global Reputation Pulse study, ethics and transparency rose in importance to their highest levels ever. Good governance—characteristic of "a responsibly run company that behaves ethically and is open and transparent in its business dealings"—moved from the No. 4 driver of reputation in 2007 to No. 2 this year.

To read an excerpt from the study, go to **bx.businessweek.com/reputation-management/**

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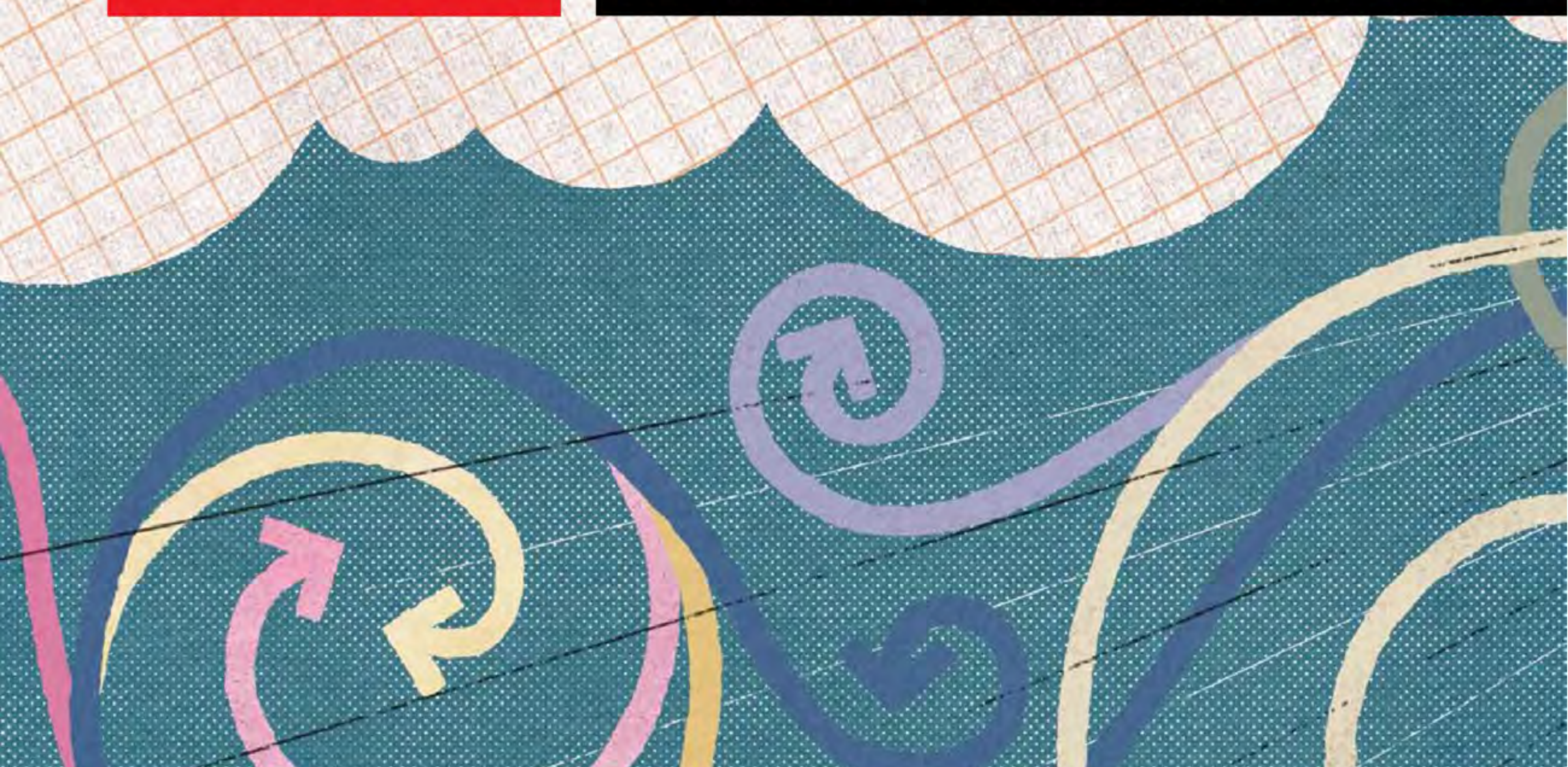
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* Samsung internal test result, compared with conventional DDR2 memory chips. Actual performance difference may vary depending on the test environment.

100 BEST GLOBAL BRANDS

TURMOIL IN THE RANKIN



By Burt Helm
Illustration by Fernando Leal

As consumers rethink their priorities, companies struggle to revamp their marketing. Here's who's coming out ahead

Last fall, as the recession deepened, Microsoft's chief marketer, Mich Mathews, got an e-mail from her team in Australia. Believing that the upbeat advertising copy supplied by headquarters was unsuited to the times, the Australians informed her they had junked it and made their own ads. Mathews recalls the Australian campaign as slapdash and off-brand; it used the glass half-empty vs. half-full metaphor to describe how business customers could save money by using Microsoft products. But Mathews had to acknowledge that the campaign made more sense in the current environment. "It was 'Hello, Mich! We need to regroup dramatically,'" she says.

The wake-up call from Down Under sent the Microsoft team back to the whiteboard. Within 21 days, headquarters had cooked up a new campaign focused on value.

The recession has presented brand stewards with the most severe test of their careers. "This is a Darwinian recession. Only the strongest will survive," says Jez Frampton, CEO of consultancy Interbrand, which computed the value of each brand in our ninth annual ranking of the Best Global Brands. Companies have had to adjust rapidly as consumers reexamine their purchases and

GS



rethink brand loyalties. Marketing executives are balancing the temptation to chase short-term gains with discounts and promotions against the risk of cheapening their brands over the long haul. Meanwhile, most have considerably smaller budgets with which to reach their customers.

Some brands have prospered amid the hard times—or at least held their own. You can read about five of them—Amazon, Pepsi, Audi, Panasonic, and Campbell's—starting on page 51.

If the ranking has one theme, it is how the mighty have fallen. While Coca-Cola kept the No. 1 spot, and Google, Amazon, and Zara continued their strong growth, UBS fell an astounding 31 places, to No. 72, losing 50% of its brand value. Seven brands fell right off the list. Among the biggest: Merrill Lynch, which ranked No. 34 last year, and AIG, previously No. 54, after both required emergency assistance from the U.S. government. ING, ranked No. 86 last year, also fell off the list after huge subprime losses. The other casualties placed near the bottom of last year's ranking and watched their prospects dim amid the recession: Hennessy, Marriott, Motorola, and FedEx.

Not surprisingly, big banks fared the worst. Several tried to win back consumers' goodwill—running ads in national newspapers defending their solvency and fiscal responsibility. But brand experts found their outreach unpersuasive. "Public-relations efforts like this are a Band-Aid," says Nancy F. Koehn, who teaches business administration at Harvard Business School. "Banks need a whole team of plastic surgeons."

EATING AT HOME

Another nonsurprise: Auto brands tanked. Two exceptions were high-end Ferrari and low-end Hyundai. Ferrari, thanks to cachet and inventory control, continued to sell its models briskly. Hyundai boosted ad spending and aggressively promoted its Assurance program, which allows buyers who lose their jobs to return cars. Hyundai's brand value slipped 5%, but it moved up three places to No. 69.

This year seven brands made the list for the first time. The seven are the apparel brands Burberry, Polo, and Puma, low-cost food companies Campbell Soup and Burger King, cosmetics maker Lancôme, and the tech firm Adobe Systems, whose Flash player is the de facto video standard on the Web.

Food brands, including Nestlé, Heinz, Pepsi, Kellogg's, Campbell's, and Danone, benefited because consumers began eating at home more. The food companies also got an unexpected windfall: Having raised prices to offset soaring commodity prices last fall, they have enjoyed higher profits since raw material prices fell back to earth.

Big Food is fighting the growing private-label threat by appearing to be anything but generic. Kellogg is boosting its advertising spending to draw attention to such new products as Special K Protein Shakes, Jumbo Multi-Grain Krispies, and Froot Loops with added fiber. Nestlé, meanwhile, has responded to consumers' newfound craving for simplicity by launching a new Häagen-Dazs ice cream line with just five all-natural ingredients.

Fashion brands also did surprisingly well this year. Several, such as Louis Vuitton and Gucci, benefited by expanding into China and the Middle East, where economies held up relatively well compared with the West. Luxury companies specializing in handbags and other accessories—including Vuitton, Gucci, and Hermès—generally performed better than those best known for apparel, such as Chanel. Accessories are simply seen as a smarter buy nowadays: Someone who splurges $1,000 on a new handbag can make use of it every day—not so for a similarly priced dress. Meanwhile, the affordable "fast-fashion" chains H&M and Zara rocketed up our list.

The recession may be abating, but life isn't going to get much easier for corporate marketing chiefs. They are already under enormous pressure to justify their budgets. And consumers are widely expected to remain frugal long after the global economy revives. "In saturated, shrinking markets," says Interbrand's Frampton, "competition becomes even tighter." |BW|

—With Matthew Boyle in New York and Carol Matlack in Paris

THE BIGGEST WINNERS

BRAND	BRAND VALUE ($ MILLIONS)	CHANGE SINCE 2008
Google	31,980	25%
Amazon.com	7,858	22
Zara	6,789	14
Nestlé	6,319	13
Apple	15,433	12
H&M	15,375	11
Ikea	12,004	10
Wrigley	6,731	10
Danone	5,960	10
Heinz	7,244	9

THE BIGGEST LOSERS

BRAND	BRAND VALUE ($ MILLIONS)	CHANGE SINCE 2008
UBS	4,370	-50%
Citi	10,254	-49
Harley-Davidson	4,337	-43
American Express	14,971	-32
Morgan Stanley	6,399	-26
HSBC	10,510	-20
Starbucks	3,263	-16
Sony	11,953	-12
Dell	10,291	-12
Lexus	3,158	-12

BUSINESSWEEK.COM | For a video on the marketing plans of firms from Ford to McDonald's, and for more on the 100 Best Global Brands, go to businessweek.com/go/brand



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100 BEST GLOBAL BRANDS

How *BusinessWeek* and Interbrand pick the winners in our annual ranking (it's way more than name recognition)

How does Interbrand compute a value for the brands that appear in *BusinessWeek*'s Best Global Brands ranking? A brand must derive at least a third of its earnings from outside its home country, be recognizable beyond its base of customers, and have publicly available marketing and financial data. Those criteria eliminate most telecoms, heavyweights such as Wal-Mart, which sometimes operates under different brand names internationally, and private companies.

Interbrand ranks only the strength of individual brand names, not portfolios of brands, which is why Procter & Gamble doesn't show up. Airlines are not ranked because it's too hard to separate their brands' impact on sales from factors such as routes and schedules. Pharmaceutical brands don't appear because consumers typically relate to the product rather than the corporate brand.

BusinessWeek chose Interbrand's methodology because it evaluates brand value in the same way other corporate assets are valued—on the basis of how much it is likely to earn for the company in the future. Interbrand uses analysts' projections, company financial documents, and its own qualitative and quantitative analysis to arrive at a net present value of those earnings. The brand values are based on data collected during the 12 months prior to June 30, 2009.

STEP ONE is calculating how much of a company's total sales falls under a particular brand. In some cases the brand encompasses nearly all sales, as with McDonald's. In others it is tied to only one set of products: Louis Vuitton within LVMH Group. Using analysts' reports, Interbrand projects five years of sales and earnings tied to each brand's products and services.

STEP TWO is calculating how much of those earnings derives from the power of the brand. Interbrand strips out operating costs, taxes, and charges for the capital employed to arrive at earnings attributable to intangible assets. Interbrand then estimates the brand's effect on earnings relative to other intangible assets, such as patents and management strength.

FINALLY, those future earnings are discounted to arrive at a net value. Interbrand discounts against interest rates and also against the brand's overall risk profile to factor in brand strength. Ingredients include market leadership, stability, and global reach—or the ability to cross geographic and cultural borders. The final result values the brand as a financial asset. *BusinessWeek* and Interbrand believe this figure comes closest to representing a brand's true economic worth. BW

RANK 2009	2008		2009 BRAND VALUE $MILLIONS	2008 BRAND VALUE $MILLIONS	PERCENT CHANGE	COUNTRY OF OWNERSHIP	DESCRIPTION
1	1	COCA-COLA	68,734	66,667	3%	U.S.	In a hard year for fizzy drink makers, Coke gained luster. Credit the *über*-successful Coke Zero, a no-cal beverage with a more macho image than Diet Coke.
2	2	IBM	60,211	59,031	2%	U.S.	IBM has strived to make itself more broadly relevant by focusing on clean air and water, more efficient health care, and mass transportation.
3	3	MICROSOFT	56,647	59,007	-4%	U.S.	For the first time, Microsoft's sales slipped. Yet it also began forcefully taking on its rivals, launching the Bing search engine and advertising hard against Apple.
4	4	GE	47,777	53,086	-10%	U.S.	GE painted itself green with its "Ecomagination" crusade. Now it aims to color itself healthy by pushing health-care solutions in underserved markets.
5	5	NOKIA	34,864	35,942	-3%	Finland	Nokia continues to lag in smartphones, but its reputation for robust construction, ease of use, and low-key style has helped it dominate mass-market handsets.
6	8	McDONALD'S	32,275	31,049	4%	U.S.	The downturn heightened the appeal of Mickey D's low-priced fare, particularly in Britain and France, while new McCafé coffee drinks have perked up sales.
7	10	GOOGLE	31,980	25,590	25%	U.S.	Its new free services are pushing it beyond search. But with trustbusters on the prowl, Google faces a challenge in maintaining a cuddly brand image.
8	6	TOYOTA	31,330	34,050	-8%	Japan	It lost money in 2008 and likely will again in '09. But deep pockets and newly focused management mean this titan should revive when the economy does.
9	7	INTEL	30,636	31,261	-2%	U.S.	Intel paid a $1.45 billion antitrust fine in Europe, but that hasn't slowed the chipmaker's push into new markets, including smartphones and home electronics.
10	9	DISNEY	28,447	29,251	-3%	U.S.	Falling attendance at its parks and sliding DVD sales are hurting. But the Mouse House continues to invest in its future, including buying Marvel for $4 billion.



MARIO ANZUONI/REUTERS

PEPSI'S WEB-SMART THRUST INTO CHINA

By Bruce Einhorn and Frederik Balfour

Its promotions have made it the No. 1 cola in the mainland



SHANGHAI

On a stage built in a disused Shanghai factory, a young bassist paces nervously, a stainless steel bicycle chain dangling from his belt. As his group prepares to perform for a standing-room-only crowd, a bandmate tilts his hat over one eye, doing his best to look like Justin Timberlake. ¶ Welcome to Pepsi's Battle of the Bands. The *American Idol*-style television show is a big component of the company's brand-building efforts in China. Some 6,000 bands tried out for 10 spots on the show, which was broadcast nationwide and streamed to Pepsi's Web site. The winner, a five-piece combo from Tianjin called Focus Point, got $30,000, a trip to a Los Angeles recording studio, a car, and a role in a Pepsi TV ad.

Worldwide, of course, Pepsi (No. 23 on *BusinessWeek*'s Best Global Brands survey) remains far behind Coca-Cola (No. 1). But by at least one important measure, Pepsi is beating its archrival in China. It's the No. 1 cola, with 23% of the soda market, vs. Coke's 22%, according to researcher Euromonitor International. The country "represents our single biggest opportunity today outside the U.S.," says CEO Indra K. Nooyi, who spent 12 days in China this summer.

Pepsi thinks the Internet is key to unlocking that opportunity. In August the company launched the "Pepsi Creative Challenge," soliciting online birthday wishes marking the 60th anniversary of the founding of the People's Republic. Last year a promotion called "Go China," before the Beijing Olympics, encouraged people to send in patriotic slogans and pictures of themselves. Pepsi got 28 million submissions and more than 122 million votes to decide the winners, whose photos and slogans were printed on soda cans. And in 2006, some 28,000 Internet users submitted scripts for a Pepsi TV ad. "Pepsi [in China] is one of the best digital marketers anywhere," says Tom Doctoroff, North Asia director for ad agency JWT.

PEPSI

CEO: Indra Nooyi

RANK: 23

DIGITAL SAVVY: The company expects its China marketing to boost juice sales, too

The promotions are the brainchild of Harry Hui, Pepsi's chief marketing officer for China. The former head of Greater China for Universal Music, Hui is serving as producer of Battle of the Bands and is one of its three judges. "Consumers in China are bombarded with messages, so merely telling them what they should drink or eat might not resonate," Hui says. "Giving them a platform where they can talk back fosters a deeper relationship with the brand."

TEMPORARY FIZZ?

Web campaigns are growing in importance for most foreign companies in the mainland. With more Chinese than Americans online, social media and blogs are "a must-have component of marketing in China," says Sam Flemming, chief of CIC, a research firm in Shanghai that works with Pepsi.

Coke, meanwhile, is no stranger to the Net, and it's turning up the heat in China, too. Pepsi may be the No. 1 cola, but it's behind Coke's Sprite, the top soda in the country. Coke's Minute Maid leads the juice segment, with 10.3% of the market, vs. just 1.4% for Pepsi's Tropicana. Coke also sponsors an *American Idol*-style competition of its own, and its iCoke Web site is a popular portal for gamers in China. "Everyone knows about iCoke," says Tony Ip, China managing director for G2, Grey Group's digital-marketing arm. Though Pepsi's big campaigns create a lot of buzz, it's short-lived, he says. "I don't see them building equity," says Ip.

Pepsi executives counter that the efforts will pay off as they move into juices and other noncarbonated drinks. But they acknowledge that marketing can get you only so far in China and that plans to boost distribution are equally important. To really succeed, says Ken Newell, Pepsi's beverage chief for the country, "we must build plants further into China." |BW|

RANK 2009	2008		2009 BRAND VALUE $MILLIONS	2008 BRAND VALUE $MILLIONS	PERCENT CHANGE	COUNTRY OF OWNERSHIP	DESCRIPTION
11	12	HEWLETT-PACKARD	24,096	23,509	2%	U.S.	HP extended its lead over Dell and weathered the economic downturn better than most tech companies, thanks to its acquisition of services provider EDS.
12	11	MERCEDES-BENZ	23,867	25,577	-7%	Germany	Although sales have plunged, the engineering icon has maintained its premium image with new fuel-efficient models. It needs to add small cars to the lineup.
13	14	GILLETTE	22,841	22,069	4%	U.S.	Brisk-selling high-end razors have boosted sales. But to extend its reach to more buyers, Gillette will have to innovate at the lower end of the market, too.
14	17	CISCO	22,030	21,306	3%	U.S.	The battle to rebrand itself as more than a maker of Web plumbing continues. By acquiring the Flip video camera, Cisco aims to be more consumer-focused.
15	13	BMW	21,671	23,298	-7%	Germany	It has demonstrated that buyers will pay a premium for a chic, sporty compact. BMW is also benefiting from an early investment in more efficient engines.
16	16	LOUIS VUITTON	21,120	21,602	-2%	France	The world's preeminent luxury brand has enjoyed a sales rebound in Europe this year, while continuing to tap new wealth in Asia and the Middle East.
17	18	MARLBORO	19,010	21,300	-11%	U.S.	As marketing restrictions tighten at home, the cigarette giant continues to push hard in emerging markets from Asia to Russia and win over millions of smokers.
18	20	HONDA	17,803	19,079	-7%	Japan	Despite slumping global sales, Honda's lineup of gas sippers and a profitable motorbike business have helped the automaker navigate the recession.
19	21	SAMSUNG	16,796	17,518	-1%	S. Korea	It has overtaken Sony as the top TV brand and emerged as the only credible challenger to Nokia in mobile phones. To expand its appeal, it is opening an app store.
20	24	APPLE	15,443	13,724	12%	U.S.	Mac sales have slowed, but Apple continues to prosper thanks to the iPhone, now in its third generation, and an app store that rivals are rushing to copy.
21	22	H&M	15,375	13,840	11%	Sweden	As many retailers suffer from the global recession, H&M has been expanding and luring value-conscious consumers with its affordable-yet-stylish apparel.
22	15	AMERICAN EXPRESS	14,971	21,940	-32%	U.S.	Hurt by accounts gone bad, the aspirational card company is bolstering loyalty programs and reviewing its card portfolio to get rid of riskier account holders.
23	26	PEPSI	13,706	13,249	3%	U.S.	It got a brand facelift with a new logo and sleeker packaging, but it was not immune to the tough climate for carbonated beverages, particularly in the U.S.
24	23	ORACLE	13,699	13,831	-1%	U.S.	Amid shrinking demand for corporate software, Oracle has stepped up face-to-face meetings—dinners, seminars—between its executives and customers.
25	28	NESCAFE	13,317	13,055	2%	Switzerland	Nestlé's flagship is playing to consumers' new aversion to pricey designer coffee. It also is catering to the health-conscious with new drinks.
26	29	NIKE	13,179	12,672	4%	U.S.	Battling to control costs and keep rivals at bay, Nike continued amid the recession to spend money on innovation, including a line of eco-friendly sports gear.
27	31	SAP	12,106	12,228	-1%	Germany	It remains the leader in providing software to automate HR and other internal corporate functions. But a new line of Web-based software has disappointed.
28	35	IKEA	12,004	10,913	10%	Sweden	The home goods giant is flourishing as recession-scarred consumers continue to snap up its stylish-yet-affordable designs, offsetting stumbles in Russia.
29	25	SONY	11,953	13,583	-12%	Japan	It has lost billions on TVs and game consoles. But Sony's software is improving: The latest e-book Reader allows users to tap Google Books and local libraries.
30	33	BUDWEISER	11,833	11,438	3%	U.S.	Squeezed at home by premium brews on one side and discount ones on the other, the beer maker is growing strongly in emerging markets such as Vietnam.
31	30	UPS	11,594	12,621	-8%	U.S.	The global downturn hit the shipping giant hard. UPS has upped its marketing budget to $200 million and is building a new hub in China.
32	27	HSBC	10,510	13,143	-20%	Britain	The worldwide credit crisis slammed its U.S. retail businesses. The world's second-largest bank is now trying to extricate itself from those bad bets.
33	36	CANON	10,441	10,876	-4%	Japan	Corporate cutbacks hurt its office machine and chip-making businesses. To rev up sales, Canon is preparing new products with more network-friendly features.
34	39	KELLOGG'S	10,428	9,710	7%	U.S.	Easing commodity costs and higher prices boosted profits, while new products like Special K Crackers and Jumbo Rice Krispies kept private label rivals at bay.
35	32	DELL	10,291	11,695	-12%	U.S.	It is continuing its overhaul by moving aggressively into retail and sharpening its design chops, but Dell needs to cut costs if it is to compete with HP and others.
36	19	CITI	10,254	20,174	49%	U.S.	Mismanagement and bad bets on risk at home have sullied Citi's reputation around the world, though its international business remains profitable.
37	37	JPMORGAN	9,550	10,773	-11%	U.S.	It is capitalizing on its position as one of the strongest financial institutions. The acquisition of Washington Mutual should give JP broader reach in the U.S.
38	38	GOLDMAN SACHS	9,248	10,331	-10%	U.S.	It proved that when the chips are down in finance, those that lose the least become the new winners. Now, Goldman is under fire over its outsize profits.
39	40	NINTENDO	9,210	8,772	5%	Japan	Its Wii and portable DS gaming consoles still outsell rivals'. But the company isn't recession-proof: Annual profits could fall for the first time in four years.
40	44	THOMSON REUTERS	8,434	8,313	1%	Canada	Since the merger, Thomson's strength in less cyclical areas such as legal information has helped balance Reuters' heavy dependence on financial services.

AT AMAZON, MARKETING IS FOR DUMMIES

By Spencer E. Ante

Instead of lavish ads, it invests in technology and distribution—and the results are startlingly effective

The world's best-known companies typically spend hundreds of millions of dollars a year on advertising and marketing to build their brands. ¶ Not Amazon.com. The giant online retailer has created one of the world's strongest brands by eschewing conventional tactics. Instead of shelling out big bucks for lavish trade shows and TV and magazine ads, Amazon pours money into technology for its Web site, distribution capability, and good deals on shipping. The result: a smooth shopping experience that burnishes the company name. "It is pretty unprecedented that their brand has ascended so quickly without a large marketing budget," says Hayes Roth, chief marketing officer at brand consultant Landor Associates. "It's not about splaying their logo everywhere. They are all about ease of use."

Amazon declined to participate in this story, in part because executives say they don't spend much time on branding. Still, the company had the biggest jump in this year's ranking of the Best Global Brands, rising 13 spots, to No. 43.

One reason is that Amazon has thrived during the recession, even as other retailers have been battered and pushed into bankruptcy. The company's reputation for offering low prices, broad selection, and quality service has resonated with strapped consumers. In the past six months, Amazon reported 16% revenue growth, while most retailers saw sales fall. "By investing back in the user experience, you get high loyalty and repeat usage," says Sebastian Thomas, head of U.S. technology research for RCM Capital Management, an investment firm with a stake in the company.

The performance is something of a vindication for Chief Executive and founder Jeffrey Bezos. After the dot-com bubble burst, critics hammered him for investing so much in technology and physical distribution centers. Some investors called for Bezos to pull back and produce more short-term profits. Now those heavy investments are paying off big time, helping the company sell an ever-widening range of products to more than 94 million customers. Amazon's stock has more than doubled over the past three years, while the Standard & Poor's 500-stock index is off about 20%. "Amazon has taken the long-term perspective," says Thomas. "Things they were criticized for have become essential assets."

There are limits to the Amazon brand. The company hasn't had much luck selling luxury items, and some expansions, such as its shoe site Endless.com, have failed to gain much traction, prompting Amazon's bid for rival Zappos in July. "They have not been successful in all categories," says Citigroup analyst Mark Mahaney.



AMAZON
CEO: Jeff Bezos
RANK: 43
SERVICE: Smooth sales and fast deliveries bring buyers back again and again

Such disappointments won't stop Amazon from new experiments, though. The company plans to dabble in conventional marketing this fall, with a national TV ad campaign. But instead of hiring a hotshot ad agency, Amazon started a contest in which anyone could create their own commercial. The company picked five finalists and then asked customers to vote for their favorite. The filmmaker with the highest average customer rating, to be announced on Sept. 21, will get a $10,000 Amazon.com gift card. "I am sure they will get a great deal of press," says Landor's Roth. "They won't have to spend a lot of money on media because they will get everyone else to do it for them." | BW |

JOHN KEATLEY/REDUX

RANK 2009	2008		2009 BRAND VALUE $MILLIONS	2008 BRAND VALUE $MILLIONS	PERCENT CHANGE	COUNTRY OF OWNERSHIP	DESCRIPTION
41	45	GUCCI	8,182	8,254	-1%	Italy	The storied luxury maker has held up better than many rivals, thanks in part to an aggressive push in emerging markets, especially brand-obsessed China.
42	43	PHILIPS	8,121	8,325	-2%	Netherlands	The conglomerate has continued a transition from low-margin electronics maker to a leading player in health care, lighting, and high-end consumer gadgets.
43	58	AMAZON	7,858	6,434	22%	U.S.	The e-tail titan prospered by continuing to offer low prices and superb customer service in hard times. It risks losing focus by expanding into e-books and apparel.
44	51	L'OREAL	7,748	7,508	3%	France	The world's leading cosmetics and mass-market beauty brand continues to reinforce its sales in emerging markets, particularly Brazil, India, China, and Poland.
45	47	ACCENTURE	7,710	7,948	-3%	U.S.	It launched an ad campaign after the crash positioning itself as "the partner of choice" in uncertain times. That didn't stop corporations from cutting consultants.
46	46	EBAY	7,350	7,991	-8%	U.S.	Once the symbol of yard-sale-style online auctions, the Web site is increasingly selling new products from wholesalers and liquidators. GM is even selling cars.
47	48	SIEMENS	7,308	7,943	-8%	Germany	A bribery scandal hurt, but the electronics maker has moved on and aims to exploit its engineering prowess in green energy and mass transportation.
48	56	HEINZ	7,244	6,646	9%	U.S.	The ketchup king now derives more than 60% of its sales overseas and plans to boost marketing spending to fend off the threat from private-label products.
49	49	FORD	7,005	7,896	-11%	U.S.	It deftly separated its brand from the troubles of its Detroit siblings. But as Ford rolls out a risky "one model for all markets" strategy, it faces a newly minted GM.
50	62	ZARA	6,789	5,955	14%	Spain	Zara is benefiting from a strong appetite for fashionable but affordable clothing. It spends relatively little on advertising, relying on word of mouth to drive sales.
51	61	WRIGLEY	6,731	6,105	10%	U.S.	The maker of gums including Orbit and Extra is getting traction by pushing the health benefits of chewing its brands.
52	57	COLGATE	6,550	6,437	2%	U.S.	Despite the global slowdown, Colgate's oral, personal, and home-care categories grew robustly this year, while the brand gained share at home and abroad.
53	55	AXA	6,525	7,001	-7%	France	The insurer is trying to project stability (new slogan: Redefining Standards) amid industry turmoil. Profits have slumped but not as much as some analysts expected.
54	52	MTV	6,523	7,193	-9%	U.S.	Pinched by sliding ratings among young adults and a drop in advertising, it is revamping its programming, including more animation and documentary series.
55	53	VOLKSWAGEN	6,484	7,047	-8%	Germany	With its lineup of fuel-efficient cars and strong positions in China and Brazil, VW has held up better than the industry as a whole. It has work to do in the U.S.
56	59	XEROX	6,431	6,393	1%	U.S.	Amid a dismal year for office equipment, Xerox forged ahead with new eco-friendly technologies and continued its move beyond hardware into services.
57	42	MORGAN STANLEY	6,399	8,696	-26%	U.S.	While trading operations have revived earnings, the brokerage business remains under siege. The firm won't regain its footing until the economy rebounds.
58	63	NESTLE	6,319	5,592	13%	Switzerland	With a nearly $2 billion R&D budget, it has moved into healthier fare—from nutritionally enriched baby food to probiotics that protect the skin from the sun.
59	60	CHANEL	6,040	6,355	-5%	France	Sales of its perfumes and apparel have suffered in the downturn, but the legendary Paris fashion house says it expects to eke out sales growth in '09.
60	66	DANONE	5,960	5,408	10%	France	The world leader in fresh dairy products looks poised for increased global reach after raising $4.3 billion—its first capital increase in 22 years.
61	64	KFC	5,722	5,582	3%	U.S.	The launch of its grilled chicken meal was a PR mess due to a coupon shortage, but the new, healthier product helped turn around declining U.S. sales.
62	70	ADIDAS	5,397	5,072	6%	Germany	Sales are declining, but thanks to strength in soccer balls, shoes, and apparel, Adidas will likely rebound in 2010 as the World Cup in South Africa approaches.
63	73	BLACKBERRY	5,138	4,802	7%	Canada	No brand has a bigger global presence in smartphones than BlackBerry. It certainly doesn't hurt that the U.S. President wears one on his belt.
64	65	YAHOO!	5,111	5,496	-7%	U.S.	After fending off Microsoft's advances, Yahoo cut a search deal with the software giant. It was needed but showed the limits of Yahoo's tech prowess.
65	67	AUDI	5,010	5,407	-7%	Germany	It has suffered less than other luxury car brands, thanks to its foothold in China and lower exposure to the U.S. market. Sharing parts with VW helped margins.
66	68	CATERPILLAR	5,004	5,288	-5%	U.S.	Construction may be quiet in the U.S., but in building sites, mine pits, and farm fields in China and India, Caterpillar's big yellow machines are multiplying fast.
67	69	AVON	4,917	5,264	-7%	U.S.	Amid a tough global economy and battle for sales, Avon has been expanding its direct-sales army—often by recruiting people laid off from other industries.
68	71	ROLEX	4,609	4,956	-7%	Switzerland	Fancy watches aren't selling like they used to. But to maintain brand integrity over the long haul, Rolex has discouraged its dealers from lowering prices.
69	72	HYUNDAI	4,604	4,846	-5%	S. Korea	Encouraged by a weak won and the improving quality of its cars, Hyundai poured money into marketing and boosted global market share to a record 5%.
70	76	HERMES	4,598	4,575	1%	France	Leather goods are holding up relatively well in the recession, especially in Asia where new stores are opening, helping the fashion house boost sales this year.

AS THE RACE SLOWS DOWN, AUDI HITS THE GAS

By Jack Ewing

The German carmaker is pouring money into marketing to expand its share of the luxury market and push diesel models in the U.S.



INGOLSTADT, GERMANY

Your industry is in the midst of a savage downturn and your competitors are slashing their marketing budgets. So what do you do? If you're German automaker Audi, you boost your U.S. ad spending by 20%, blow $6 million or so on a Super Bowl spot, and even sponsor television coverage of Barack Obama's inauguration. "We took the crisis as a huge opportunity," says Peter Schwarzenbauer, the Audi management board member in charge of marketing.

The contrarian approach seems to be paying off. The Volkswagen unit edged upward on this year's Best Global Brands list, to 65 from 67, while archrivals Mercedes-Benz and BMW slipped (though both still outrank Audi). More important, Audi's global sales have held up reasonably well, falling just 7.5% through August, vs. 17% at Mercedes and 18% at BMW. Audi benefited from its relatively fuel-efficient lineup and its strong position in China, where sales are still growing.

In fact, the financial crisis has been pretty good to Audi. In Europe this year the automaker has outsold Mercedes and BMW, a huge milestone for a brand that was close to extinction in the 1960s. In the U.S., Audi sold 8,000 cars in August, up 26% from the year before. For 2009, its share of the U.S. premium market has risen to 8.2% from 6.5%, though American sales are still down 10%. Globally, Audi aims to be the leading premium brand by 2015.

AUDACIOUS AD

Audi's 60-second spot during the Super Bowl was a not-so-subtle declaration of war on competitors. In a series of chase scenes, a suave action hero fleeing a bunch of bad guys cracks up a Mercedes and a BMW before finally escaping at the wheel of an Audi A6 coupe. The message: Those other brands have had their day. Now it's Audi's turn.

That's an audacious attitude for a company that still sells fewer than half as many cars in the U.S. as either of its German rivals. Equally bold is Audi's strategy of pushing its fuel-efficient diesel engines. Diesel cars have traditionally been a tough sell in the U.S., where the fuel is usually more costly than gasoline and filling up may entail queuing patiently behind big rigs. But the company says its research shows that a third of U.S. drivers would buy diesels, which can be as efficient as hybrids. To reinforce the message, a spot now running on American TV depicts barrels of oil rolling through streets before rumbling up the ramp of a cargo ship. If a third of Americans drove diesel cars, the ad claims, the U.S. could send back 1.5 million barrels of imported oil daily. "Diesel—it's no longer a dirty word," says the voiceover.

Audi's biggest problem may be restive U.S. dealers. The automaker wants to raise its profile with sleek new showrooms sporting silver-mesh facades and curvaceous windows. But given the recession, some dealers are balking at the $1 million-plus expense. Howard Cooper sells Audis, Volkswagens, and Porsches in Ann Arbor, Mich. "All three brands want new investments in dedicated showrooms and staff, and it's a tough time to do that," Cooper says. For its part, Audi argues that the new design not only looks cool, but also cuts operating costs 30% by saving space and energy. "You have to convince the dealers it's a win for them as well," says Schwarzenbauer. | BW | *–With David Kiley in Ann Arbor, Mich.*

AUDI

CEO: Rupert Stadler

RANK: 65

DRIVING VISION: Audi aspires to be the leading premium brand within six years



JOHANNES SIMON/GETTY IMAGES

RANK 2009	2008		2009 BRAND VALUE $MILLIONS	2008 BRAND VALUE $MILLIONS	PERCENT CHANGE	COUNTRY OF OWNERSHIP	DESCRIPTION
71	74	KLEENEX	4,404	4,636	-5%	U.S.	It's doing well overseas, but private labels spell trouble at home. The brand is fighting back with technology, including the Kleenex Facial Tissue with Lotion.
72	41	UBS	4,370	8,740	-50%	Switzerland	UBS brought in a new CEO to clean house, but is still struggling with the legacy of huge credit-crunch losses and revelations it helped U.S. clients evade taxes.
73	50	HARLEY-DAVIDSON	4,337	7,609	-43%	U.S.	A hog is the ultimate discretionary buy, not ideal in these times. And as boomers age, Gen Y isn't picking up the slack. Harley is pinning its hopes on Asia.
74	75	PORSCHE	4,234	4,603	-8%	Germany	A takeover struggle with VW hurt Porsche's image, and sales plunged amid the downturn. But the company still enjoys a reputation for fast, sexy, reliable cars.
75	78	PANASONIC	4,225	4,281	-1%	Japan	Its TV and digital camera units are struggling. Acquiring Sanyo Electric gives Panasonic more green products, from solar panels to batteries for electric cars.
76	80	TIFFANY & CO.	4,000	4,208	-5%	U.S.	A strong dollar and weak economy slammed U.S. sales. But Tiffany continues to open stores, and a diamond-encrusted cell phone attests to the brand's ambition.
77	79	CARTIER	3,968	4,236	-6%	France	Cartier's loyal high-end customers, particularly those living in China and the Middle East, have softened somewhat a consumer pullback elsewhere.
78	77	GAP	3,922	4,357	-10%	U.S.	Sales fell because Gap failed to lure enough shoppers to its low-priced apparel. Featuring its four divisions on one Web site also could confuse consumers.
79	81	PIZZA HUT	3,876	4,097	-5%	U.S.	Sluggish sales in the U.S. have prompted the pizza chain to turn to China and India for growth as it expands its menu with new dishes such as pasta and wings.
80	92	JOHNSON & JOHNSON	3,847	3,582	7%	U.S.	J&J has long been perceived as comforting and trustworthy—ideal positioning for hard times. Its sponsorship of the 2008 Olympics boosted its global visibility.
81	82	ALLIANZ	3,831	4,033	-5%	Germany	The insurer preserved a reputation for financial solidity by avoiding the worst of the crisis. Allianz is poised to grow as it moves into markets such as India and China.
82	83	MOET & CHANDON	3,754	3,951	-5%	France	Consumers switching to cheaper champagne and sparkling wines have hurt. With fewer marketing dollars, it is doing things like film festival sponsorship.
83	84	BP	3,716	3,911	-5%	Britain	The oil giant has brought new projects online, mollified Russian partners, and focused green energy efforts on a few businesses such as wind power in the U.S.
84	89	SMIRNOFF	3,698	3,590	3%	Britain	Tony beverages suffered as consumers cut back on boozing, but Smirnoff held its own with cheaper libations and premade cocktails.
85	88	DURACELL	3,563	3,682	-3%	U.S.	Beset by private labels, new ads invoke a heritage of safety, trust, and performance. It is also innovating, including a battery charger that works in a car.
86	98	NIVEA	3,557	3,401	5%	Germany	Sales fell in the U.S. and Europe as consumers switched to generic skin-care products. Nivea is using its brand strength to win loyalty in emerging markets.
87	91	PRADA	3,530	3,585	-2%	Italy	Armed with fresh capital, the only fashion label with a movie named after it is opening stores around the globe.
88	93	FERRARI	3,527	3,527	0%	Italy	Ferrari sales typically have held up in good times and bad. This recession is no exception, prompting the carmaker to open new stores and launch new models.
89	94	ARMANI	3,303	3,526	-6%	Italy	Despite offering fashion at various price points, Armani has so far avoided hurting its brand. Now it is developing a chain of luxury hotels and resorts.
90	85	STARBUCKS	3,263	3,879	-16%	U.S.	Hit by the recession and facing competition from McDonald's, the chain is making its food healthier, lowering some prices, and introducing, yes, instant coffee.
91	NEW	LANCOME	3,235	New	New	France	Thanks to such innovations as a "vibrating power mascara," plus a handful of celebrity endorsements, the cosmetics giant has regained some of its luster.
92	97	SHELL	3,228	3,471	-7%	Netherlands	Its reputation restored after a scandal over misrepresenting oil reserves, the company is cutting layers of management to match lower oil prices and profits.
93	NEW	BURGER KING	3,223	New	New	U.S.	Cheeky ads and the Whopper Bar, which offers customized burgers, bolstered BK's appeal. To maintain momentum next year, its ad budget will rise 25%.
94	100	VISA	3,170	3,338	-5%	U.S.	The company is poised to capitalize on a growing global shift from high-cost credit cards to debit cards. Visa already dominates the U.S. debit-card market.
95	NEW	ADOBE	3,161	New	New	U.S.	Designers of ads and Web sites swear by its software, which includes Flash and Photoshop. But tough times have hurt sales of Adobe's latest products.
96	90	LEXUS	3,158	3,588	-12%	Japan	The recession and stiff competition from European rivals hurt Lexus, which is hoping its emphasis on hybrid models will differentiate it from the pack.
97	NEW	PUMA	3,154	New	New	Germany	The sneaker maker is accelerating a push into fashion by, for example, joining with British designer Alexander McQueen in an attempt to compete with Adidas.
98	NEW	BURBERRY	3,095	New	New	Britain	Like many luxury brands, it is looking for new customers in emerging markets, including Bahrain. Burberry also opened a new office in New York City.
99	NEW	POLO RALPH LAUREN	3,094	New	New	U.S.	Sales have slumped, but an elegant new Web site and increasing emphasis on reaching younger consumers have helped the apparel maker beat expectations.
100	NEW	CAMPBELL'S	3,081	New	New	U.S.	The 140-year-old company has found success by pitching its soups as cheap, nutritious meals. It aims to expand its offerings in Russia next year.

The brand valuations draw upon publicly available information, which has not been independently investigated by Interbrand.
Valuations do not represent a guarantee of future performance of the brands or companies.

Data: Interbrand, *BusinessWeek*



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PANASONIC PUTS ITS CHIPS ON 3D TV

By Ronald Grover and Kenji Hall

Plasma sets have given it a big boost. Now it's betting consumers will pay up for 3D

All consumer electronics companies have to draw attention to themselves in an ever-more-cluttered marketplace. Incremental improvements on familiar products won't do the trick these days. Panasonic, which ranks 75th on our list of the Best Global Brands, will take its chances on bringing to the living room a technology just catching on in movie theaters. Hello, 3D television. And 3D video and digital cameras, Blu-ray players, and more. "This is the biggest thing out there for us, says Eisuke Tsuyuzaki, the chief technology officer of Panasonic's North American Operations. "As a business, 3D has a huge potential bang for the buck."

PANASONIC

CEO: Yoshi Yamada

RANK: 75

COMING AT YOU: The new TVs will be promoted alongside the eagerly awaited 3D film *Avatar*

Panasonic is known for its high-quality, large-screen plasma televisions, which helped it shore up its U.S. market share during the Great Recession (even as it and every other competitor watched prices fall by as much as 30%). But recently, the company, which makes everything from light bulbs to refrigerators, has been trying to create an even higher brand profile.

Last year the former Matsushita Electric Industrial renamed itself Panasonic. It was a no-brainer because the Panasonic brand has a reputation for technological prowess and could cast a halo over the stodgy Japanese leviathan.

Panasonic has been building up the brand ever since. It won praise for its Viera high-definition TVs, which were the first sets able to stream shows and movies from the Web without any additional equipment. Then right after the launch of the TVs, the company started a service called VieraCast, which allows viewers to watch videos from YouTube and Amazon.com on the Viera sets. Panasonic also set up a social network, livinginhd.com, where Viera fans and other early adopters can get glimpses of new products, trade information, and share complaints, too. The company claims it has more than 70,000 members.

Panasonic gained prominence among a broader audience when it landed a coveted spot as an official sponsor of the 2008 Democratic National Convention. It provided 200 high-definition TVs (including three 103-inch monsters behind the podium where Barack Obama accepted the nomination of his party).

Sometime next year, the company plans to introduce its 3D sets so that couch potatoes can watch 3D movies and sporting events in all their eye-popping glory. Panasonic won't be the first out there with 3D: Samsung, Mitsubishi Electric, and Texas Instruments sell 3D-ready sets now. But Panasonic will have a big marketing advantage. The company has a deal with 20th Century Fox to help promote the eagerly anticipated 3D film, *Avatar*, directed by James Cameron and due to be released in December. Panasonic has begun a worldwide advertising campaign, featuring the film along with its 3D TVs and Blu-ray players.

Panasonic, of course, hopes 3D will go mainstream, as HDTV did, and cast a glow over the entire brand. But 3D sets will be pricey, at least for the first few years. (Panasonic won't give details.) And viewers will have to wear battery-operated glasses to get the full effect. It could be a hard sell. | BW |

MICHAEL NAGLE/REDUX

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100 BEST GLOBAL BRANDS

CAMPBELL'S: NOT ABOUT TO LET THE SOUP COOL

By Matthew Boyle

The recession has proved a boon, but to stay dominant the company is launching new products and wooing the Russian market

In tough times, comfort sells. And few brands evoke a warm and fuzzy feeling more than Campbell's, whose soup has been a staple since the late 19th century. The cost-conscious climate has been a boon for soup sales, which rose 5% in the U.S. in fiscal 2009, way better than the 1% growth of 2008. That performance launched Camden (N.J.)-based Campbell Soup into the ranks of the top 100 brands, where it joined food giants Kellogg, H.J. Heinz, and Nestlé.

But as the recession recedes, CEO Douglas R. Conant will need to prove that Campbell's name still resonates with American consumers, many of whom will venture back into restaurants once the economy improves. To stay on top, he's launching new products, recasting old favorites, and aggressively pushing into emerging markets. "We've developed a much better understanding of how to keep our brand relevant," says Denise Morrison, president of Campbell's North American soup, sauces, and beverages.

Consider Campbell's Chunky line of soups. Last year the company neglected the brand, focusing instead on Select Harvest, a new offering aimed at women over 35. Select Harvest became one of the top food launches of 2008. But Chunky suffered as a result: Its ad budget got slashed 25% last year, according to data tracker TNS Media Intelligence.

Now Campbell's is revamping Chunky, the first major overhaul of the product in a decade. The company wants to make the soup more nutritious without sacrificing its perceived heartiness. More than half the line now has an extra dose of vegetables and lean meat. "We're not talking about tofu here," says Morrison. The company also plans to advertise Chunky in women's magazines, a departure from testosterone-laden marketing efforts of the past that featured pro football stars.

China and Russia present a bigger opportunity—and a bigger challenge—for Campbell's. The two countries account for more than half the world's consumption of soup. But nearly all of it is homemade. If the company can capture just 3% of the at-home consumption, says Larry S. McWilliams, president of Campbell's international group, the size of the business would equal that of the U.S. "The numbers blow your hair back," he says.

CAMPBELL'S

CEO: Doug Conant

RANK: 100

SUPER BOWL: The idea is to make sure soups don't slump when people eat out again



To break into those markets, Campbell's has been conducting extensive on-the-ground research over the past few years, interviewing thousands of consumers in Russia alone. McWilliams even asked the mother of Campbell's local marketing director for her feedback. (She wanted to see more fat medallions floating around.) Their findings led them to develop a broth-like product that Russians can use as a base for their own soups. Next year the company will sell 14 different soups in the country, up from three this year.

Campbell's has had more success in Russia than in China, where tastes vary by province. But the company says it could start showing a profit in those countries by next year. If so, the gains could guard against a U.S. soup slump. Says UBS analyst David Palmer: "The make-or-break time for them is now." |BW|

CHRIS CRISMAN


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064 When your VC drops you
066 The trouble with investor lawsuits
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WHAT'S NEXT

FINANCE

How Real Is the Rally In Real Estate Bonds?

Big investors are scooping up mortgage securities and bidding up their prices—but the easy money may have been made



ROBERT NEUBECKER

By Christopher Palmeri and Theo Francis

As the U.S. Treasury laid out plans to bolster the housing market last spring, Chimera Investment jumped into action. The New York real estate investment trust raised \$1.45 billion in two stock sales and used the proceeds to scoop up distressed mortgage-backed securities for as little as 50¢ on the dollar. Chimera figures it can earn double-digit returns on the bonds, even if many of the underlying home loans aren't paid back. "Our latest offering is now fully invested," Chimera CEO Matthew Lambiase said in a conference call this summer. "The early results are promising."

After warily circling the market for months, big investors such as Chimera are bulking up on residential mortgages and the investments filled with them. The additional demand, sparked by a modicum of good news in housing and government purchases of the securities, has helped drive up prices on such bonds by as much as 30% since March. But will the rally last?

So far this year mortgage-related REITs have raised \$4.6 billion from investors. Among the recent initial public offerings: PennyMac Mortgage Investment Trust, founded by former Countrywide executive Stanford L. Kurland. Even banks are getting into the game, aggressively buying government-backed mortgage bonds just as they consider selling some of their junkier holdings.

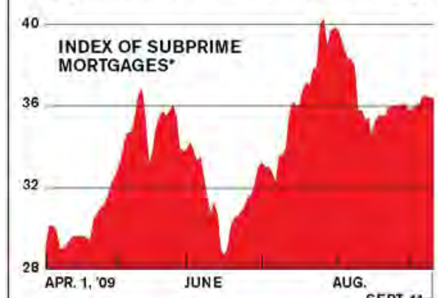
HOW TO PLAY IT 076

Some players are betting on the housing market, which is showing signs of life. Home sales were up 7.2% in July. And the Standard & Poor's Case-Shiller U.S. National Home Price Index climbed 1.4% from May to June. As recently as December, home values were falling at twice that pace. "People are feeling pretty good and wondering whether the worst is over," says Bryan Whalen, a mortgage fund manager at Metropolitan West Asset Management.

Other investors are chasing government dollars, which are flooding the mortgage market and boosting prices. The Federal Reserve is little more than halfway through its commitment to buy \$1.25 trillion worth of securities sold by the troubled mortgage giants Fannie Mae and Freddie Mac. As part of a public-private partnership designed to cleanse toxic assets from banks' books, the U.S. Treasury will pony up as much as \$30 billion to

RISKY RALLY

The junkiest loans have risen sharply



*Markit ABX.HE Index created in July 2006 as a benchmark for credit default swaps of AAA tranches of subprime mortgage-backed securities.
Data: Markit



money managers, funds they can use to buy old mortgage investments.

The federal funds have motivated Kevin E. Grant, CEO of Cypress Sharpridge Investments. His New York-based mortgage REIT, which raised $100 million in an IPO, is focused on securities backed by the government. Grant says he can collect a tidy profit on the bonds: Their yields hover around 4.25%, while his borrowing costs stand at 2%. "[Mortgages] are the largest opportunity I've seen in my entire lifetime in any industry in the world," says Grant.

BOON FOR BIG BANKS

The rush of investors is only pushing prices higher. The junkiest bonds, those that invest in subprime and other risky mortgages, have jumped by 30% since March. Some of the higher-quality securities are trading at 100¢ on the dollar, or par, a sign that investors think there's little or no risk the home loans won't be repaid.

Big banks are benefitting. The troubled firms own $1.3 trillion worth of mortgage securities, roughly 10% of their total assets. Those bonds, which have been a drag on their books for a while, are showing gains. According to an analysis for *BusinessWeek* by investment bank Keefe, Bruyette & Woods, more than 360 banks reported an increase in the value of their mortgage-backed securities in the second quarter. The portfolios of both Fifth Third Bancorp and Comerica rose 2% in the period. "It strengthens their balance sheets," says Frederick Cannon, director of research at KBW.

Given the price spikes, some analysts figure the banks may decide to start cleaning up their books and offloading the riskiest securities they own. "You'll see them selling securities, residential loans, construction loans," says Mark T. Fitzgibbon, director of research at Sandler O'Neill & Partners, a brokerage firm. The firms had been reluctant to sell in a depressed market, since it would have meant taking a big writedown.

For investors, the easy profits may be gone. Some analysts worry that the Fed will lose its appetite for mortgage securities now that housing is on the mend. Already, there's speculation the central bank won't reach its $1.25 trillion goal. Such fears, founded or not, could spook buyers, sending shock waves through the market.

The other wild card: housing, wherein the fundamentals remain weak. As unemployment rises, more borrowers may fall behind on their mortgage payments, potentially triggering losses in the securities that contain the loans. Each 1% rise in the annual jobless rate will cause another 1.2% of mortgages to go into foreclosure, estimates Stan Liebowitz, an economics professor at the University of Texas at Dallas. Says Jeffrey Gundlach, chief investment officer at money manager TCW: "The claim that housing is out of the woods is greatly exaggerated." |BW|

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Commercial Market Woes

The commercial real estate market, which typically lags the residential one, continues to deteriorate. Commercial property deals, notes a Bloomberg piece, are expected to fall to the lowest level in almost two decades. About $16 billion of office transactions will be completed by yearend, according to data compiled for the media outlet by Real Capital Analytics, a New York research firm.

To read the full article go to **http://bx.businessweek.com/commercial-real-estate/reference/**

When Your Venture Guy Says Goodbye

As VC firms struggle to raise money, partners are leaving—and startups are being left in the lurch

SMALL BIZ

By Eileen Gunn

Hubert Engelbrechten, CEO of Fremont (Calif.) semiconductor manufacturer GTronix, has helped raise $40 million in venture capital for his company, including a $10 million round led by Jafco Ventures in Palo Alto, Calif. Jafco partner Aaron Cheatham was instrumental in persuading his firm to invest in GTronix and became one of the company's board members. But in the fall of 2008, Cheatham dropped a bombshell: Jafco had become disenchanted with the semiconductor industry, and Cheatham would be leaving the firm to become a consultant.

For entrepreneurs, unexpected exits such as Cheatham's raise unnerving questions about the possibility of a replacement board member, access to the VC firm's network, and the availability of follow-on financing. Such departures are becoming more common as venture firms have trouble raising money or stop investing in certain industries.

"Quite a few of my clients have been told that a firm is no longer investing in their sector, so the partners who focus on it are leaving," says Josh Nathanson, a partner with Cleveland recruiter ON Search Partners. And with many portfolio companies struggling, venture firms are quicker to cut loose a partner who brings in problematic deals.

In 2008 the number of principals at VC firms shrank almost 16%, according to the National Venture Capital Assn. Mark Stevens, a partner at Mountain View (Calif.) law firm Fenwick & West, says the issue of departing directors "is one I've been dealing with more in the last 12 months, and I'm in a space that's pretty healthy—digital media." He continues: "With the disruption in the venture industry, it's only going to happen more."

That disruption has been severe. VC firms raised just $1.7 billion in the

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second quarter of 2009. That was the smallest amount since 2003 and nowhere near the high of $32.5 billion raised in the second quarter of 2000. And a survey by Deloitte Touche Tohmatsu found that 21% of firms are changing the sectors they fund. Entrepreneurs in semiconductors and electronics appear to be most vulnerable, as some 50% of venture capital firms plan to cut back there over the next three years. Other mature, cash-intensive industries, such as telecommunications and pharmaceuticals, are also being pinched.

At GTronix, Engelbrechten needed to make sure Jafco was still committed. "I knew we would need more funding to get us through the downturn," he says. He invited his new director, Nick Sturiale, to the company's offices for a briefing and tour and had him attend his first board meeting while Cheatham was still there. In the first quarter of 2009, with GTronix beginning to bring in revenues, Jafco led a $7 million round of funding for the company.

But there are more difficult outcomes, too. Santa Clara (Calif.)-based Quellan, another of Cheatham's semiconductor companies, was acquired in August by Intersil, a publicly traded semiconductor manufacturer. "I thought there would be additional [venture] financing, but it's too hard to build an independent company in sectors that are capital-intensive," says Cheatham. "This way the firm got something of a return." Quellan CEO Tony Stelliga says the sale was a tough call: "You're at a point where your technology risks are behind you, you have good prospects, customers, and market momentum," he says. On the other hand, "there's not much going on in the IPO market, so your exit is less certain. But that's what happens with startups." | BW |



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Do Shareholder Class Actions Make Sense?



JUSTIN MAXON/THE NEW YORK TIMES/REDUX

Not when they extract payments from innocent shareholders and let fraudsters off the hook

COMMENTARY

By Michael Orey

When New York Federal District Court Judge Jed S. Rakoff rejected a proposed $33 million securities fraud settlement between the Securities & Exchange Commission and Bank of America on Sept. 14, he pointed out that the money would come out of the pockets of BofA investors—meaning that "shareholders who were the victims of the bank's alleged misconduct [would] now pay the penalty for that misconduct."

The settlement agreement aimed to resolve allegations that, during its acquisition of Merrill Lynch at the end of last year, BofA concealed information from investors about Merrill's plan to pay up to $5.8 billion in bonuses to its executives. Rakoff said the SEC didn't adequately explain why it had not pursued charges directly against the bank executives or lawyers allegedly responsible for issuing "false and misleading" proxy statements and instead targeted the corporation. In his order nixing the deal, he called it "unfair," "unreasonable," and "inadequate."

222

The number of federal securities class actions filed in 2008

Data: Stanford Law School/ Cornerstone Research

Rakoff's ruling prompts a question that seems to garner little attention outside a small circle of academics: Why do we tolerate the same perverse approach and empty outcomes in the resolution of private shareholder class actions? These lawsuits, typically filed by institutional investors, are independent of any government action and seek to recoup shareholder losses allegedly caused by a company providing false or incomplete information to the market. The value of settlements in such cases can dwarf those obtained by federal and state regulators, and there is widespread agreement among legal scholars that these class actions make little economic sense and are anemic deterrents to fraud.

Yet, while exacting little if any price from the executives and corporate advisers who led investors astray, this litigation costs corporations (read: shareholders) dearly. Even excluding the mega-cases of Enron, WorldCom, and Tyco International, businesses paid out $21 billion to settle investor claims in the five-year period from 2004 through 2008, according to Cornerstone Research. (Including those cases, the amount was $42 billion.) On top of that companies can pay their defense lawyers upwards of 20% of what they shell out in settlements.

On the same day Judge Rakoff issued his ruling, President Barack Obama made a speech on Wall Street, stressing his Administration's plan to enact "the most ambitious overhaul of the financial system since the Great Depression." While proponents of shareholder class actions have long held them up as a vital supplement to government enforcement—a way to add thousands of cops to the regulatory beat and compensate the wronged—a close look at private suits filed in the BofA-Merrill deal reveals the illogic of these claims.

SHAREHOLDER VS. SHAREHOLDER

Just weeks after BofA closed its acquisition of Merrill on Jan. 1, investors saw the value of their shares plummet when it was revealed that Merrill's losses for 2008 were $27 billion, far higher than anticipated. The shareholder claims almost all involve "aftermarket" investors, who bought and sold from one another in the secondary market, not directly from the corporation through a stock offering. So BofA investors who sold for a loss after Merrill Lynch's financial plight became known are now seeking payment from BofA investors who didn't sell or who acquired their shares after the price drop. Total losses haven't been specified, but collectively investors are seeking to recoup billions.

The age-old purpose of fraud claims is to force a wrongdoer to cough up ill-gotten gains to the person deceived. Shareholder lawsuits do no such



Judge Rakoff called the BofA settlement "unfair" and "unreasonable"

thing. "An aftermarket fraud causes no transfer of wealth from an innocent victim to a guilty perpetrator of the fraud," noted Stanford University law professor and former SEC Commissioner Joseph A. Grundfest in a filing in an unrelated proceeding. "Instead, it causes a wealth transfer among equally innocent third parties." Other critics have referred to this as "circularity" or "pocket shifting."

On June 30, Judge Rakoff's courthouse colleague, U.S. District Court Judge Denny Chin, designated a group of five pension funds to lead the proposed class action in the case against BofA. While the SEC seeks to mete out discipline—through civil, not criminal proceedings—the case spearheaded by the pension funds seeks compensation for investor losses. As if having one group of investors pay another isn't odd enough, the situation gets even more twisted. Securities filings show that a number of funds sold a portion of their BofA shares but continued to hold large positions in the bank after the mid-January stock drop. Some, like the Teacher Retirement System of Texas (TRS), were also big holders of Merrill shares, which as of Jan. 1 were converted into BofA stock. The result: A portion of any compensation they get will come from themselves.

There's another reason to question the idea of allowing investors to collect for securities fraud losses. Even though neither side in an aftermarket transaction participates in the fraud that inflates the price of a stock, the seller still benefits, while the buyer loses. A number of scholars contend that investors who are diversified in the market (as is common) will on average be the beneficiaries of fraud as often as victims. This means that, over time, their gains and losses will net out at close to zero. It also means that any recovery in a lawsuit is likely to be an undeserved windfall. TRS, for example, wants money back for its losses allegedly caused by BofA's fraud. Yet last year, TRS sold shares in SunTrust Banks during a time when another lawsuit alleges SunTrust's share price was artificially high because of fraud. (BofA and SunTrust say the fraud allegations are without merit.)

The contradictions and costs of shareholder class actions as a means to compensate investors for fraud-related losses might be deemed acceptable if they effectively served another key social goal—deterring fraud in the first place. It's hard to find anybody (outside the plaintiffs' bar) who thinks they do.

Why? Because the costs of litigation, including settlements and attorneys' fees, are generally paid for by the corporation's shareholders, not the executives who committed the fraud. And settlements of investor class actions are so routine, either because they are costly to fight or because a company doesn't want to risk a potentially massive jury verdict, that they carry little or no opprobrium. After all, in settlements of shareholder suits—just as with the SEC's proposed deal with BofA—the defendants do not admit any wrongdoing. No cost to the perpetrators, no shame—where's the deterrence?

Any comprehensive reform of the financial system should include a fundamental reconception of shareholder lawsuits. Rather than compensating secondary-market investors, their aim should be to deter fraudulent conduct. That means directors and officers need to be far more than just titular defendants—they need to have skin in the game. |BW|

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Lose Some, Win Some

A number of legal scholars have noted that, over time, diversified investors will gain from securities fraud as often as they lose. A 2005 report by Navigant Consulting concludes that large institutional investors who recover their losses through litigation end up being overcompensated because they are not required to give up their gains.

To view the report, go to **bx.businessweek.com/securities-exchange-comm-sec/reference/**

MANAGEMENT & LEADERSHIP

EDITED BY JENA McGREGOR



C-SUITE

Who Needs COOs?

During a recession, when efficient, lean management is at a premium, chief operating officers would seem to be in hot demand. But the ranks of CEO deputies are dwindling. Executive search firm Crist/Kolder Associates has found the percentage of COOs in big companies is at a 15-year low and the rate of decline has been sharper in 2009 than in any year since 2001.

It's not because of headcount trimming: Rather, says John Keller, a senior client partner at executive search firm Korn/Ferry International, boards are shunning big-picture visionaries for "operationally astute" chief executives, while CEOs want less separating them from the business. Plus, as many CEOs stay on as chairmen when a new chief executive is named, says management consultant Jay Galbraith, these executive duos see less need to add a second in command.

But one unspoken reason COOs' numbers may be falling, says Galbraith, may be simple fear. As the pressure on CEOs heats up, at least a few simply don't want such an obvious successor in place.

MULTINATIONALS

Testing Managers' Global IQ



Companies increasingly screen potential leaders for everything from personality traits to emotional intelligence. But the next measure for moving up the ladder may be global IQ.

Researchers at Thunderbird School of Global Management have developed a 91-question exam to assess employees' "global mindset." Managers at Intel China, LG Electronics, Raytheon, and others are currently using it as a self-assessment tool to determine how likely they are to thrive in global roles, according to Mansour Javidan, the professor who designed the study.

An analysis of responses from the 6,000-plus executives who have taken the test thus far found that scores improve when an overseas stint stretches to two years, but a one-year posting isn't much better than six months. And managers under the age of 40 and over the age of 65 scored higher on the exam than those aged 40 to 64. "Whatever the explanation," Javidan says, "the biggest concern with that finding is that group is the one running the world right now."

BENEFITS

More Coverage for Domestic Partners

As companies cut back on benefits, one perk is on the rise: domestic partner benefits. Last year the Human Rights Campaign (HRC), a nonprofit devoted to lesbian, gay, bisexual, and transgender (LGBT) equality, found that 17 companies in its annual study of 590 corporations and law firms added the benefit, bringing the total to 554.

HRC measures treatment of LGBT employees by calculating a score that incorporates things like whether LGBT staffers are included in the equal employment opportunity policy. The number of companies that scored 100 rose 17%, to 305.

ExxonMobil was the lone large company to score zero. HRC says it lost points for opposing a shareholder resolution that called for explicitly adding sexual orientation and gender identity to its equal employment policy. ExxonMobil says it does not tolerate discrimination, but federal law does not demand that its policy include those groups.

COMPANY	2007 REVENUE RANK	2010 CEI RATING
Wal-Mart Stores	1	40
Exxon-Mobil	2	0
Chevron	3	100
General Motors	4	100
Conoco Phillips	5	70

Data: Human Rights Campaign Corporate Equality Index

ILLUSTRATIONS BY MARK TODD


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The Boy Toy Maker Chasing Barbie

With its new line of Liv dolls, Spin Master brings its cool stylings to the tough girls' market

By Christopher Palmeri

Can three guys who came out of nowhere to steal a big chunk of the lucrative—and elusive—market for boys' toys find success among the sugar-and-spice set? The founders of Toronto-based Spin Master are about to find out. Their new Liv line of dolls, launched in July, is aimed at girls aged 6 to 10.

If Liv's journey from the design lab to store shelves is any indication, the doll market is tougher than Spin Master had realized. "The odds," says Needham analyst Sean McGowan, "are against any new product succeeding."

Walk into the bedroom of any boy under the age of 10, and you're likely to twist an ankle on a Spin Master product. Thanks to such hits as Bakugan Battle Brawlers (a line of magnetic action figures) and the Air Hogs line of model planes, privately held Spin Master's annual revenue has soared sevenfold over the past eight years, to more than $700 million, even as the overall toy industry has shrunk.



Spin Master has succeeded in part because founders Ronnen Harary, Anton Rabie, and Ben Varadi, who met at the University of Western Ontario in the 1990s, think like boys. Their main goal: making toys that are cool. Spin Master says its Tech Deck finger-size skateboards are among the most confiscated items in elementary school classrooms. The Havoc Heli swoops around a room like a real helicopter.



But the doll market is famously difficult to crack. Barbie has fought off dozens of rivals during her five-decade reign as the industry's top doll. MGA

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Varadi, Harary, and Rabie with examples of their boys' toys; below left, the new Liv doll

Entertainment had a hit with the Bratz dolls, launched in 2001. In 2004, Mattel sued: A jury last year ruled that Mattel, not MGA, owns the Bratz line because the dolls' designer was working for Mattel when he created them. Retailers quickly shunned the Bratz brand, and sales collapsed. MGA is appealing the verdict.

With the litigation swirling, Spin Master decided to get into the doll market. In 2006 it paid an undisclosed sum to an outside designer for a doll prototype with an internal mechanism that allowed it to move its arms and legs freely. Focus groups of girls told the mostly male development team that they didn't much care for a fashion robot. "The girls' aisle is so different," laments Chief Creative Officer Varadi.

Back at the drawing board, Spin Master completely reimagined the prototype. It took out the motors and added wigs. It gave its characters—four high school friends—backstories and imperfections that make them seem more real than the aspirational Barbie astronauts, beauty queens, and Presidential candidates. Spin Master also created a Web site, Livworld.com, where the dolls' diaries are updated daily, allowing it to weave new products into the story lines.

In July, Spin Master finally released Liv, and so far the results have been positive: The $19 toys have become top sellers at Walmart.com and are the No. 2 doll at Target in terms of shelf space, according to Kloster Trading analyst Lutz Muller.

Still, if dollmakers have learned anything over the years, it's that the whims of little girls are unpredictable. "If it doesn't work," says McGowan of the Liv line, "you may not ever know why." | BW |

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FIRST IN A SERIES

THREE FACTORS KEY TO WORKPLACE WELLNESS

This year, employers will pay about $9,600 for health insurance per worker — an increase of 6% over 2008, according to Towers Perrin's annual Health Care Cost Survey. But companies that offer their employees high-performing onsite health and wellness programs will spend an average of $1,200 less, a substantial savings over time.

According to Towers Perrin, these companies are encouraging employees to take better care of themselves by building a culture of health and wellness, educating them about optimal use of their health plans and sponsoring health-boosting activities.



But motivating employees to make the lifestyle changes required to significantly reduce healthcare expenditures — most notably increased physical activity and a more wholesome diet — is notoriously difficult. The key ingredients of a high-performing program are senior management involvement, flexibility and accessibility, says Peter Hotz, president of Take Care Health Employer Solutions Group, a Walgreens Health and Wellness Company.

Senior management involvement: Top executives need to show that fitness is important to them, says Hotz, who has joined office teams in activities such as a triathlon and a 45-mile charity bike ride.. "It has to start at the top," he says. "Senior management has to believe in it, has to live it, has to model it." Take Care Health Employer Solutions Group, part of the Walgreens family since May 2008, provides employee health and wellness programs as well as onsite healthcare in the form of primary care, pharmacy and occupational health services. Many of its top executives "live" the fitness mission, at least one of them hitting the stairs to Take Care Health's 14th-floor offices every day.

Flexibility: A flexible program, Hotz says, takes into account the fact that a company may employ both ultra marathoners and people for whom climbing a few flights of stairs is a challenge. You need to offer programs that meet the needs of both ends of the fitness spectrum.

Accessibility: Lastly, Hotz says an accessible program offers many different ways for employees to participate, from offering an onsite gym and wellness programs or simply endorsing noontime walks for time-pressed employees who might otherwise not feel they can get away from their desks.

A successful program, says Hotz, "depends on where the company is in their evolution of health and wellness," which starts with awareness of the benefits of good health and identification of individual health risk factors with an annual health assessment. It goes on from there to educate workers on how to mitigate those risk factors through participation in health and wellness activities.

Take Care Health Employer Solutions' results speak for themselves. One worksite that uses its wellness programs and other services was able to identify more than 300 employees with high blood pressure, a major risk factor for many conditions. Now, a year later, almost half of those employees have achieved normal blood pressure.

Hotz says every company is different and requires a customized program to suit its unique workforce, something he says sets Walgreens apart from others in the marketplace. In addition to its worksite health and wellness centers, Walgreens is helping organizations achieve positive outcomes through its broad portfolio of capabilities that span from in-store clinics to specialty pharmacy and infusion services.

Whatever the approach a company chooses, Hotz says to expect cultivating a culture of health and wellness to take several years. "You can't just snap your fingers and expect behaviors to change overnight," he says. "You have to do it as a long-term investment. It is a process and a journey."

~ Story by Mary Van Beusekom

Look for more articles on leadership in health and wellness in upcoming issues of BusinessWeek.



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MONEY REPORT

A P&G REBOUND?

11%

Decline in P&G's share price so far this year

Data: Bloomberg

Shares of Procter & Gamble gained 4.2% on Sept. 10 after the consumer-products giant announced it expects product sales, not including the impact of acquisitions and foreign exchange, to grow 1% to 4% next quarter. That represents an abrupt turnaround for P&G, which has suffered for much of the year. (The company said it still expects sales to fall as much as 3% during the current quarter.) ¶ P&G's sales are being driven by price cuts as well as marketing outlays that could exceed $500 million by next summer. In Turkey, for instance, the company cut prices to reflect the fall in the Turkish lira—and regained the eight percentage points of market share it lost earlier in 2009. ¶ At 55.03, Procter & Gamble shares remain cheap even after that 4.2% rise, says UBS analyst Nik Modi. The stock is down 11% so far this year, compared with a 16.5% gain by the Standard & Poor's 500-stock index. Modi expects that situation to reverse—if P&G can "deliver on its promise. And I'm pretty confident they can," he says. The stock should trade around 70 within the next 12 months, Modi says. –*Ben Levisohn*



STOCKS

THE RIGHT DIRECTION

More and more smartphones offer a navigation application that gives a driver, cycler, or walker turn-by-turn directions. Bad news for dedicated navigation device makers like Garmin and TomTom? Not necessarily.

On Sept. 10, Bank of America Merrill Lynch analyst Vivek Arya upgraded Garmin from "underperform" to "buy" and set a target price of 45. On Sept. 14, the company's stock closed at 36.81. Arya cites, among other things, overwrought concerns about consumers adding "nav apps" to smartphones rather than buying Garmin's device. But such issues as screen size, battery life, and the cost of the apps seem to be working against their use in smartphones. Another positive for Garmin is dealers' need to restock inventory in the wake of the cash-for-clunkers program.

The company is also benefiting from an expanding market in aviation, marine, and fitness/bicycling—segments that account for about 30% of Garmin's sales and some 45% of its operational earnings. On Sept. 11, Goldman Sachs added Garmin's Dutch rival, TomTom, to its "conviction-buy list" of stocks it expects to outperform the Standard & Poor's 500-stock index, with an 18-month price target of 17 euros, up from 10 euros. –*David Kiley*

MEXICO

BOLSA BOOM

Mexico's Bolsa Index hit a 15-month high on Sept. 15. Despite the government's budget woes and an economy forecast to shrink 7.7% in 2009—the biggest decline since the 1930s—"the worst appears to be over," says Citigroup analyst Eduardo Estrada Lopez.

That's good news for Wal-Mart de México, whose shares make up about 14% of the index. Lopez expects the stock to rise about 10%, to 54 pesos, as it gains market share. HSBC analyst Richard Dineen is bullish on wireless operator América Móvil, which makes up 22% of the Bolsa. He has a target of 40 pesos; the stock trades at 31.

The fund T. Rowe Price Latin America has more than 20% in Mexican stocks. It's up more than 100% since March, but Morningstar analyst William Samuel Rocco says it "has a longer-term focus" than rivals. Still, the fund is risky: It lost 56% in 2008.
–*Tara Kalwarski*



Mexico's stock exchange is at a 15-month high

(BOTTOM RIGHT) AFP PHOTO/RONALDO SCHEMIDT



ARTHUR GIRON

How Real Is the Rally In Real Estate Bonds?

(FROM PAGE 062)

By Amy Feldman and Christopher Palmeri

A slew of financial heavy hitters, including Starwood Capital's Barry Sternlicht, Colony Capital's Thomas Barrack Jr., and Apollo Global Management's Leon Black, are piling into the distressed-mortgage market. They and other savvy real estate investors have been setting up real estate investment trusts to raise funds to buy mortgages and mortgage-backed securities. But is the timing right for these REITs?

Since the start of the year, four new real estate investment trusts have raised $1.8 billion, according to Renaissance Capital, a Greenwich (Conn.) firm that tracks initial public offerings. An additional 18 are in the works, with plans to raise $6 billion. Investors should proceed with caution, says financial planner Harold Evensky. He adds: "I get nervous whenever Wall Street touts something as *the* hot product."

Distressed investing requires a strong stomach. More than 13% of home loans were delinquent or in foreclosure in the second quarter, according to the Mortgage Bankers Assn. For subprime loans, that number was 40%. Meanwhile, delinquencies of commercial mortgage loans—which tend to trail their residential counterparts—topped 4% in August, compared with less than 1% the year before, according to Trepp, a provider of data about commercial mortgage-backed securities (CMBs).

Adding to risk now is that the market for residential and commercial mortgage bonds—especially, the AAA-rated ones—has rallied strongly since its March lows. "A lot of money is chasing an asset whose fundamentals haven't changed," says Thomas Atteberry, co-manager of FPA New Income Fund. "We think it is somewhat early to do this." But while AAA-rated bonds are up sharply, many BBB-rated ones still trade for less than 20¢ on the dollar. As Manus Clancy, a senior managing director at Trepp, says of the low-rated CMBS: "I think people are pricing them to the worst-case scenario."

While the spotlight has been on the residential market, the commercial market may offer better opportunities. One reason is uncertainty over how the government's role in home loan modifications might change. Two of the most experienced distressed investors, Colony and Apollo, target commercial mortgages.

An alternate, far riskier approach is the one taken by PennyMac, which is run by a former executive of onetime mortgage giant Countrywide Financial. It buys portfolios of home loans from banks and the Federal Deposit Insurance Corp. PennyMac has its own loan servicer, which seeks to renegotiate its distressed loans to avoid foreclosures.

Investors should check the manager's expertise, of course—particularly if it will need to negotiate with homeowners facing foreclosure. They should also consider that some REITs have hedge fund-like fees—1.5% management fees plus a significant share of any profits.

A more cautious way to invest is through mutual funds such as TCW Total Return Bond Fund. It returned 14.6% over the past year. Perhaps tellingly, manager Jeffrey Gundlach has been reducing exposure to riskier nonagency bonds (bonds not backed by Fannie Mae or another quasi-governmental institution) as the mortgage market has rallied. | BW |

THE RUSH TO REITs

Four mortgage REITs have gone public in 2009; 18 more are in the pipeline. Here are some of note:

ALREADY PUBLIC
Cypress Sharpridge Investments/CYS
PennyMac Mortgage Investment Trust/PMT
Starwood Property Trust/STWD
IN THE PIPELINE
Apollo Commercial Real Estate Finance/ARI
Bayview Mortgage Capital/BAY
Brookfield Realty Capital/BKF
Colony Financial/CLNY
Marathon Real Estate Mortgage Trust/MRE

Data: Renaissance Capital

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MUTUAL FUNDS

THE BEAUTY OF BOUTIQUES

By Lewis Braham

If you call the Chicago office of the Bruce Fund, chances are one of its two co-managers—Robert Bruce or his son, Jeffrey Bruce—will pick up the phone. They are, after all, the fund's only employees. Yet despite this dearth of personnel—or perhaps because of it—the $200 million fund, which can invest in almost any kind of stock or bond, has delivered a 17% annualized return over the past 10 years, beating 99% of all mutual funds. Jeffrey Bruce thinks that knowing the fund's success depends entirely on him and his father makes a difference. "If you have your name on the door, you tend to care a little more," he says.

The Bruce Fund is a classic case of what might be called the boutique-fund effect: Small, often family-run mutual fund shops can produce superlative returns. This is especially true if the shop runs only one fund. Instead of selling a multitude of investment products that cover just about everything under the sun, managers at single-fund boutiques devote all of their time and energy to making their one fund succeed. For such managers, running a fund isn't just a job. It's their primary business, their lifeblood. If that fund fails, so does their business.

Since their livelihoods are at stake, boutique managers tend to be more risk-averse and holistic in their approach to investing. Instead of investing in a specific sector and trying to beat a specific benchmark, managers often aim to make money any way they can and to keep losses to a minimum. They pursue what is called "absolute returns." This requires a more flexible investment style than big fund shops generally allow. A manager may invest in, say, Treasury bonds during a bear market and tech stocks or junk bonds during a bull run.

Finding solid boutique funds takes some work. You can screen for top funds at research site Morningstar.com, but it pays to visit the fund's home page. At RooseveltInvestments.com, for instance, you will find background information about the Sheer family, which runs the $120 million Roosevelt Multi Cap Fund. Lead manager Arthur Sheer ran money for Britain's Rothschild family for nine years before founding his firm, Sheer Asset Management, in 1990. Sons Adam and David are Sheer's president and chief financial officer, respectively. The Sheers now manage money for members of the Roosevelt family and other wealthy clans.

Although the Roosevelt fund was launched in 2001, the Sheers have been running $3.7 billion



The Roosevelt team (left to right): President Adam Sheer, analysts Nainesh Shah and Jason Sheer, and CFO David Sheer

PETER YANG

Small, often family-run mutual fund shops—especially those with only one fund—can produce superlative returns



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for privately managed accounts in the same style since the firm's founding. Since October 1990, the average annualized return for those private accounts has been 11.2%, vs. 9.2% for the stock market. In the past five years the mutual fund has delivered a 6.2% annualized return, besting 90% of its peers in Morningstar's mid-cap growth fund category.

Like the Bruce family, the Sheers practice a flexible, go-anywhere style and try to capture all of the stock market's upside while suffering less of its downside by hedging their positions or going into cash. Over the past decade their All-Cap Core Equity Composite, which tracks private accounts managed in the same style as the multi-cap fund, has beaten the market by 17% during bull markets and fallen only 73% as much during declines. "My father has always worried about the downside," says Adam Sheer. "When most people walk into a crowded theater, they think: 'I wonder if this is a good movie.' He thinks: 'My god, what if there's a fire?'"

The best boutique managers invest heavily in their funds. "All my liquid assets are in the fund or in separate accounts managed in the same style," says Adam Sheer. The same is true for the Bruce Fund. "My father is the largest shareholder in the fund, and I am No. 3 or 4 if you include my wife and kids, who are also invested," says Jeffrey Bruce.

While a flexible investment style is popular, some boutique managers aim to excel in a niche. Stralem Equity Fund buys only large-cap blue-chip stocks. Fund adviser Stralem & Co., founded in New York in 1966, is also largely a family-run business. Two families hold four of the slots on the eight-member team. Employees of the firm own more than 15% of the outstanding assets invested in the $93 million mutual fund. The firm also manages $2 billion in the same style in private accounts. Over the past 15 years the private accounts have delivered an average 11.4% annualized return net of fees, vs. the Standard & Poor's 500 index's 6.9%—and with less volatility than the market.

90%

Portion of mid-cap growth funds Roosevelt Multi Cap Fund bests with its 6.2% annualized five-year return

Data: Morningstar

NIMBLE PLAYERS

Small-cap stock funds are popular with niche boutiques. One reason for this is liquidity. Tiny companies can be difficult to trade, especially if a manager works for a big fund family with a lot of assets to invest. Positions can take longer to build or eliminate, and buying too many shares of one company can drive up the stock's price, causing the manager to overpay. A boutique house can be nimbler investing in such companies.

Walthausen Small Cap Value Fund takes full advantage of its small size. With just $12 million in the fund (the entire firm has about $90 million in assets), manager John Walthausen recently built significant positions in cookware manufacturer Lifetime Brands and Lydall, a maker of thermal insulation and filtration devices, in less than a week. "Both companies have market capitalizations below $100 million," he says. "If I were managing $1 billion, it would be very hard for me to invest in such tiny companies in a way that would make a difference to the portfolio." Although Walthausen's fund only launched in February 2008, he ran Paradigm Value Fund from January 2003 through July 2007, earning a 28.8% annualized return, which trounced the 18.5% return of his small-cap value benchmark and his peers.

Another solid niche boutique play is Conestoga Small Cap Fund. The $60 million fund launched in 2002, but managers William Martindale Jr. and Robert Mitchell have been managing money in private accounts in the same style since 1998, delivering a 7.8% annualized return since then. That compares with 0.3% for their benchmark, the Russell 2000 Growth Index.

Many boutique funds, including the Bruce Fund, must be bought directly from the company. Stralem is available through some discount brokers. If the funds have a drawback, it's that small, undiscovered funds may not gather enough assets to survive. Unsuccessful funds can get liquidated quickly, perhaps not giving managers enough time to prove themselves. But the flexible approach of many of these funds, as well as the large personal stakes their managers often have in them, help tilt the odds in their favor. |BW|

LITTLE GEMS

FUND NAME	5-YEAR RETURN*	NET ASSETS (MILLIONS)
Bruce Fund/BRUFX	7.5%	$200
Conestoga Small Cap/CCASX	3.3	60
Roosevelt Multi Cap/BULLX	6.2	120
Stralem Equity Fund/STEFX**	3.0	93
Walthausen Small Cap Value/WSCVX***	N/A	12

*Annualized returns as of Aug. 30, including capital appreciation plus reinvestment of dividends
**Institutional share class; new retail share class symbol: STRAX
***Launched in 2008 Data: Morningstar, fund companies



SPRINT—WITH OR WITHOUT A BUYER

The spate of merger-and-acquisition activity in recent weeks is boosting Wall Street's optimism, and more deals are in the pipeline. The most recent buzz is about Sprint Nextel (S), the third-largest U.S. telecom. Speculation that Deutsche Telekom, which owns T-Mobile, is eyeing Sprint gave Sprint's shares a boost.

SPRINT'S RECENT UPTICK



Data: Bloomberg

The rumors lifted the stock to 4.15. Then it eased to 3.98 on Sept. 16. (Sprint sank to 1.35 last November.) But even if no deal occurs, the stock is still a buy, says Chandan Sarkar of investment firm Auriga USA. He notes that Sprint is trading below its asset value, which he pegs at 5 to 10 a share. However, if a merger does materialize, he says it would be a "strong long-term positive" because it would reduce the number of competitors in an "overly crowded sector."

A deal would benefit both [Sprint and DT] "as it would allow leverage against the two largest carriers [Verizon and AT&T] and reduce price competition," says James Moorman of Standard & Poor's. He notes that Sprint, which he rates a buy, is trading at an "attractive valuation" and offers a valuable subscriber base. Aside from initiating cost-cutting measures that he says have been bearing fruit, Sprint has introduced several new handsets, such as the Pre, with price plans designed to attract new subscribers.

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BRAD TRENT; CHARTS BY DAVID FOSTER

TYCO'S STEADY OOMPH



Data: Bloomberg

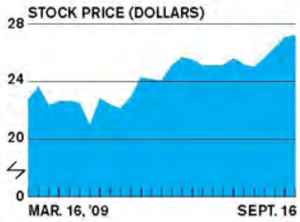
More Security For Tyco

Tyco International (TYC) is no longer a glamour stock since it spun off its electronics and health-care arms in 2007. Even so, the No. 1 maker of electronic security gear is showing lots of oomph. On Sept. 16 it hit 34.42, up from 18 in March.

As the economy stabilizes, Tyco is likely to reach 45 in a year, says John Inch of Bank of America Merrill Lynch, which has done banking for Tyco. He says 2009 will be a trough for profits at Tyco. Even so, he has revised his 2009 earnings forecast to $2.32 a share from $2.18, and expects $2.65 in 2010 and $3 in 2011, vs. 2008's $3.06.

Tyco may also consider selling its steel tubing and cable products unit (11% of sales), says Nicholas Heymann of investment firm Sterne, Agee & Leach, who tags Tyco a buy. Providing a push, he says, are a likely share buyback and higher payouts—currently the dividend yield is 2.46%.

THE SHINE ON ALBERTO-CULVER



Data: Bloomberg

Alberto-Culver Looks Alluring

Will Alberto-Culver (ACV), the fourth-largest U.S. maker of personal-care products, including VO5 and Nexxus, do an acquisition or agree to be bought out? Analysts are sure it will be one or the other since Alberto-Culver currently has $500 million in cash, or about $4.67 a share.

That robust balance sheet could be a source of "value creation," allowing Alberto to acquire another company or brand, says Jon Anderson of investment firm William Blair (it owns shares), who rates the stock outperform.

Dara Mohsenian of Morgan Stanley believes Alberto, whose stock has risen to 27.21 from 20 in April, is an attractive mid-cap player as the beauty-products industry consolidates. As such, it deserves a "consolidation premium," says Mohsenian, who rates the stock outperform. An Alberto spokesman says the company is always on the lookout for strategic acquisitions. |BW|

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*As of August 2009

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OUTSIDE SHOT | JEFFREY E. GARTEN

The Case for a Global Central Bank

With world finance increasingly intertwined, we'll need one sooner or later





When the finance ministers and central bankers of the world's 20 largest economies gather in Pittsburgh on Sept. 24, they can congratulate themselves for averting a 1930s-type meltdown. But nothing the G-20 has done, or is likely to do, will prevent or substantially moderate the next global crisis. That will require deep-seated, global financial reforms. And for such change to take root, something else will be needed: the establishment of a global central bank.

I can hear the howls of critics. World Government! A Conspiracy of Bankers! In the U.S. Congress the aversion to such an institution would make the dogfight over health care look like a genteel dinner party. So right now there is zero chance that the U.S.—and other countries, such as China, that zealously guard their sovereignty—would support the idea. But if critics could suspend the hyperventilating for a few minutes, they'd realize a global central bank is becoming a necessity in today's complex, interconnected world economy.

Why? Think about the responses to previous financial meltdowns—the Latin American debt crisis of the 1980s, the Asian financial crisis and the collapse of Long-Term Capital Management in the 1990s, the Internet stock implosion early in this decade. Following each crisis, governments

(FROMTOP) DAVID JOHNSON; ILLUSTRATION BY EMILIANO PONZI

promised to create new rules and institutions—a fresh "financial architecture," in the parlance of pundits. But little was done. As a result, each successive crisis has been worse than the last. Each has involved more countries and asset classes. Each has been more globally synchronized. Each has more clearly shown that private financial institutions compete too fiercely for markets and profits to regulate themselves. Bottom line: The cost of failing to implement a global structural response—the lost economic growth, the lives destroyed—has escalated dramatically.

At the heart of this reality is a simple fact: Governmental oversight remains national, while financial institutions are more globally intertwined. No top official denies this dichotomy. Jean Claude Trichet, president of the European Central Bank, recently bemoaned the lack of international coordination needed to manage the "deeply integrated global economy." U.S. Treasury Secretary Timothy Geithner warned that "we need a common global solution to these markets, not separate regional solutions."

As the current credit crisis has shown, the degree of global interconnectedness in finance is astounding. According to McKinsey, annual cross-border capital flows increased to \$11.2 trillion in 2007, more than 20% of global gross domestic product. That's up from \$1.1 trillion, or 5.2% of global GDP, in 1990. Far-flung investors own one in three of the world's government bonds, one in four stocks, one in five corporate bonds. And some \$450 trillion worth of impossible-to-value derivatives is sloshing around the globe.

The G-20's agenda correctly identifies many of the problems. But executing and sustaining oversight, especially as the recovery reduces the pressure to take painful steps, is what counts. And the record shows that the reaction of governments working together, even in good faith, is too slow, diffuse, and compromised by national political pressures to result in anything but actions that are too little, too late.



EMILIANO PONZI

How would a global central bank do better? Here are some of the ways:

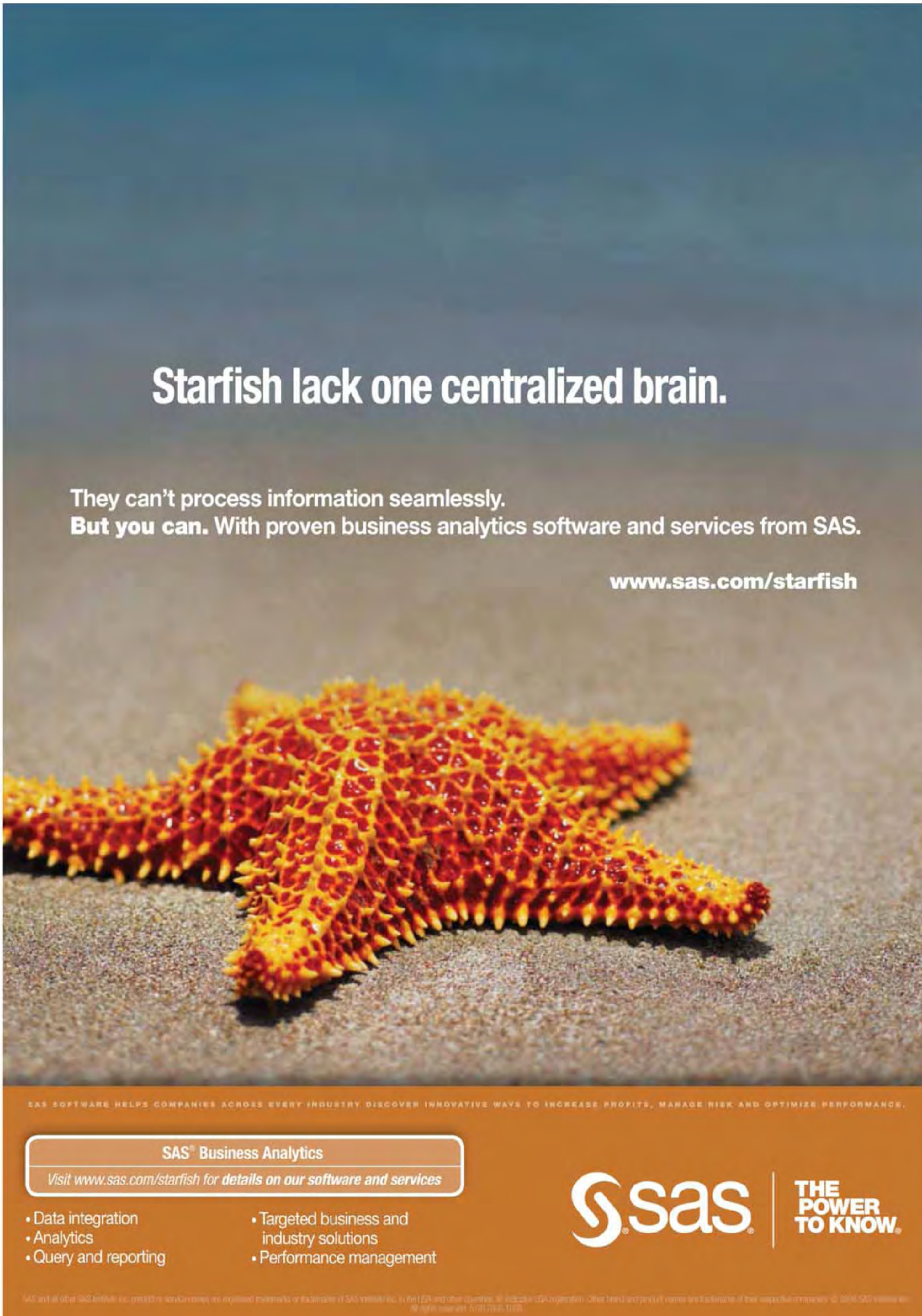
First, the bank would be the focal point for bringing together the different regulatory approaches of the U.S., the EU, and China in such areas as the oversight of banks and hedge funds, the quantity and quality of reserves, and the relationship of risk management to executive pay. We're a long way from resolution on these issues.

A global central bank would also oversee any major financial institution—a bank, securities firm, insurer, hedge fund, private equity firm, or sovereign or commodity fund—whose failure could bring down the system. (About two dozen of these exist today.) It would be responsible for restructuring these institutions, if necessary, or safely winding them down. Had such oversight existed before Lehman Brothers' collapse, the credit crisis might have been far less cataclysmic.

Another job: setting standards for debt-to-equity ratios for the biggest institutions. Past efforts, accords known as Basel and Basel II, took ages to conclude and were outdated before the ink was dry. We need a sustained process for pushing banks to acquire more reserves in boom times, the better to weather the inevitable downturns.

Currently, no central bank or finance ministry has the ability to look at such key determinants of growth and stability around the world, let alone the clout to sound alarms that would be heeded. (Or the motivation: The tendency is to try to give one's own institutions an edge.) But if a global central bank had existed before the meltdown, banks might not have been free to take on \$35 of debt for every \$1 of equity—and much less deleveraging would thus have been required in the crisis' aftermath. So lending in the past 18 months would have been less restrictive.

Finally, a worldwide central bank would engage in crisis simulation—running scenarios to heighten awareness of new dangers and sharpen the responses of government and private financial players. Such exercises in 2005-07 might have helped us anticipate how quickly a problem such as the subprime mess could spread. We are still desperately in need of such war-gaming. A new crisis could emanate from China's opaque financial


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system. Or we may need to prepare for a major currency debacle as Washington acquires trillions in new debt without a visible way of servicing it beyond devaluing the dollar.

Now for what a global central bank wouldn't do, at least until it was well established: It wouldn't create a global currency but would manage instead a world of dollars, pounds sterling, euros, yen, and renminbi. It wouldn't set monetary policy for individual nations, leaving that to existing central banks. Other questions remain, of course. To whom would this global regulator be accountable? How would it be funded? What would be its relationship to the IMF and the Bank for International Settlements (a club for central banks, albeit it a weak one)?

Outside of finance, the world has already moved toward stronger global institutions. Without a World Trade Organization, bringing China into the global trading system and managing its growing clout would have been much tougher. Absent a World Health Organization, we could not have contained SARS and other epidemics. And soon we'll need a world environmental agency to deal with climate change and other issues that far exceed the governing capacity of any one country.

Unfortunately, we are probably years away from high-level discussions about a global central bank. At its meeting the G-20 won't announce the formation of a panel of experts to study the idea. But it could do worse than create such a commission at some point. Sooner or later—perhaps after the next crisis, or the one after that—there will be an acknowledgement that the time has come for a global central bank. | BW |

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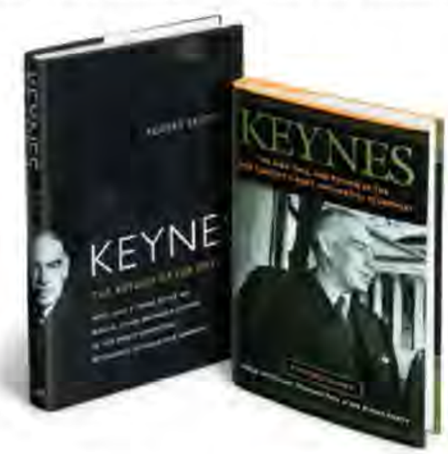
The Redemption of Keynes

Rediscovering the man whose ideas helped avert economic collapse

Thanks to extraordinary actions by the Federal Reserve, a record-breaking stimulus package, and massive bank bailouts, the downward momentum of the Great Recession has been halted. A year after the collapse of Lehman Brothers, there's no hyperbole in saying a depression was barely averted. And as the economy tentatively moves from contraction toward recovery, John Maynard Keynes ought to be named Man of the Year. Governments around the world have successfully, if messily, resurrected many of his insights from the 1930s to thwart economic collapse. Foremost is his idea that easy money and government spending can rescue an economy in free fall—with credit frozen, businesses panicked, and consumers paralyzed.

The return of Depression-era economic realities lies behind a resurgence of interest in the man. Modern macroeconomics is widely considered to be the house that Keynes built. He was a dominating transatlantic intellectual and policymaking force from World War I through World War II. (He died in 1946.) Yet by the 1990s, Keynes was largely ignored by economists, who became increasingly enamored with market efficiency and obsessed with the deadweight costs of government. Whenever action was called for to offset a slump, most economists recommended a dose of monetary policy. Politicians rarely invoked his name, and when they did it was often with disdain.

But attitudes change during a siege. As N. Gregory Mankiw, a Harvard economics professor and adviser to President George W. Bush, put it: "If you were going to turn to only one economist to understand the problems facing the economy, there is little doubt that the economist would be John Maynard Keynes."



Keynes: The Return of the Master by Robert Skidelsky; PublicAffairs; 221 pp.; $25.95

Keynes: The Rise, Fall, and Return of the 20th Century's Most Influential Economist by Peter Clarke; Bloomsbury Press; 211 pp.; $20

Two new books attempt to bring him back into focus. *Keynes: The Rise, Fall, and Return of the 20th Century's Most Influential Economist* is by Peter Clarke, a former history professor at Cambridge University, where Keynes also taught. The other is Robert Skidelsky's *Keynes: The Return of the Master*. Emeritus professor of political economy at the University of Warwick, Skidelsky earlier penned a three-volume Keynes biography (published in 1983, 1992, and 2000) that runs to more than 1,500 pages.

Both authors combat the caricature of Keynes as a market-hating, deficit-embracing, tax-and-spend socialist. And both argue that Keynes deserves better than to be trotted out only in times of crisis and that his ideas are relevant in the current debate over reforms. In this, Skidelsky's book excels. It's a passionate polemic that

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makes a strong case for economists and policymakers to reread their Keynes. He puts great stock in one of Keynes' most famous quotes: "The ideas of economists and political philosophers, both when they are right and when they are wrong, are more powerful than is commonly supposed. Indeed the world is ruled by little else."

Keynes' is a rich story, and Clarke's book emphasizes the details of his life. A product of Eton and Cambridge, he was a multitalented genius living at the center of Britain's academic, journalistic, government, financial, and artistic communities. Keynes worked in the India Office and the British Treasury and ran an insurance company. He had homosexual relationships as a young man and was later happily married to ballerina Lydia Lopokova. His literary career was deeply influenced by his membership in the Bloomsbury group, which included Virginia Woolf and E.M. Forster. In 1923 he put the income from his writing to work in the markets, making and losing several fortunes. He lived, as Clarke writes, off "the fluctuating performance of his investments."

The orthodoxy of the time held that government should do little to stop downturns. Many of the best economists of the era, such as Joseph Schumpeter and Friedrich Hayek, valued depressions as necessary purgatives. Keynes would have none of it: He saw millions of unemployed workers, their livelihoods and hopes dashed on an adherence to balanced budgets, the gold standard, and unfettered trade. This is the Keynes most of us know.

But Skidelsky brings another Keynes alive. Keynesian economics, he argues, has at its core a deep appreciation of market psychology and—unlike the efficient-market camp—uncertainty. If you can't predict the future, Keynes reasoned, then you need a system that can handle breakdowns. Writes Skidelsky: "Underlying the escalating succession of financial crises we have recently experienced is the failure of economics to take uncertainty seriously."

Skidelsky also makes a plea for economics to again become a humanist discipline. People have started asking: What is economics for? To Keynes, it wasn't about efficiency or wealth-building. He thought hard about how economics relates to an ethical life, to art and beauty, to what is truly good and valuable. And his return may create room in the post-recession debate for questions along those lines. |BW|

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What Went Wrong

In a Sept. 2 article in *The New York Times Magazine*, Nobel laureate Paul Krugman gives his take on why economists failed to see the current crisis coming. He chronicles the decline of Keynesianism, from Milton Friedman's monetarism through the missteps of Alan Greenspan: "As memories of the Depression faded, economists fell back in love with the old, idealized vision of an economy in which rational individuals interact in perfect markets, this time gussied up with fancy equations."

To read Krugman's piece, go to **bx.businessweek.com/economic-analysis/reference/**

A NEW DAWN IN LEIPZIG '89

A celebration of democracy, including prayers for peace and a festival of lights



Back in 1982, when a few hardy souls first braved the baleful eyes of the Stasi to say a prayer for peace in Leipzig's Church of St Nicholas, nobody could have imagined that this gathering would one day lead to a revolution. But their courage ultimately proved infectious. In September 1989, the prayer meetings grew into regular Monday demonstrations, and the number of participants swelled by the week. By 9 October that year, there were 70,000 people on the streets of Leipzig, chanting, "We are the people" and "No to violence". Despite the vast numbers involved, the demonstrations remained peaceful – and paved the way for a new era in Europe. Just one month later, the Berlin Wall came down. On 9 October, Leipzig will remember those historic days with a wide-ranging programme of events. And you are invited to join in the commemorations, at "A new dawn in Leipzig ´89".

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What Could Make the Zune Zoom

Microsoft's new high-def rival to the iPod may become a great game player

For the past three years, Microsoft's Zune has chased Apple's iPod. It has been a hopeless race in which the Zune, despite an attractive design, aggressive pricing, and a decent music service, has never won more than a minuscule share of the market. Microsoft, nothing if not persistent, is hoping to change the game with its newest Zune by exploiting links to the one big success story from its Mobile & Entertainment Devices group: the Xbox. You share downloaded movies and TV shows between the Zune and the Xbox, but more important, the new Zune HD could be a game machine. Unfortunately, we'll have to wait for Microsoft and its partners to provide some actual games and other applications before we can judge the potential of the excellent hardware.



Zune's most striking feature is its display, based on organic LED technology

In theory, at least, connecting the Xbox community to the Zune HD (named for high-definition video capability and HD FM radio) creates a bond with 30 million households that have purchased the game consoles. Two-thirds of them have active accounts with Xbox Live, a subscription service that lets members buy or rent movies and TV shows through Netflix and from the Xbox Live Video Marketplace, which Microsoft rebranded the Zune Marketplace. Xbox Live also provides access to Facebook, Twitter, and YouTube. The Apple TV settop box offers some of these capabilities, but its sales have been a fraction of the Xbox's.

The Zune HD ($220 for 16 gigabytes, $290 for 32) is quite an attractive piece of hardware, a bit smaller, thinner, and lighter than an iPod Touch. Its most striking feature is a gorgeous 3.2-in. touchscreen display based on organic light-emitting diodes, a technology just moving from screens in cameras and phones to larger displays.

Hardware, however, isn't the point. The Zune HD, no matter how spiffy, is not going to beat the iPod straight up as a media player. Apple is largely standing pat with its iPod lineup for the holiday season, but it has trimmed prices on the Touch, undercutting the 16 GB Zune HD by $30. It's also matching some of the Zune's best new features. Before Microsoft could even announce its Smart DJ, which combs through your music to create a continuous playlist of songs similar to those by an artist you have selected, Apple came up with the Genius playlist, which does more or less the same thing. For subscribers to Microsoft's $14.95-a-month Zune Pass service, those songs come not only from your collection but from the entire Zune catalog, something Apple, which disdains subscription music, can't offer.

To make the Zune HD a gaming whiz, Microsoft must encourage developers to offer new versions of Xbox hits

The Touch, which is really a Wi-Fi-only iPhone without the phone, is far more than a music and video player: The thousands of apps available from the iTunes Store make it a versatile handheld computer—and an excellent game platform.

The big question is whether the Zune might grow up to match and even beat the iPhone and Touch if software developers give it programs that show off its powerful hardware. Games could be the secret weapon if Microsoft can get developers, including its own Game Studios, to create Zune versions of successful Xbox titles. In fact, with its great display, motion sensing, and a speedy Nvidia Tegra processor, the Zune HD could be the best handheld game platform out there. Microsoft promises games, including Project Gotham Racing from Microsoft Game Studios. But as of the Sept. 15 launch in the U.S., apps were limited to a handful of casual games and a calculator.

The battle for music players is over. Game, set, and match to Apple. We have moved into a new round of competition involving much more powerful and versatile devices. Apple has a big lead and will be tough to catch in this market, too. Microsoft at last has built a worthy contender, but it will have to move faster on the software side to have a fighting chance. |BW|

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BusinessWeek (USPS 080 900)
SEPTEMBER 28, 2009 (ISSN 0007-7135) S T Q ISSUE NO. 4148
Published weekly, except for one issue in January, February, March, July and August by The McGraw-Hill Companies, Inc. **Founder:** James H. McGraw (1860-1948). Periodicals postage paid at New York, N.Y., and at additional mailing offices.
Executive, Editorial, Circulation, and Advertising Offices: The McGraw-Hill Companies Building, 1221 Avenue of the Americas, New York, N.Y. 10020. Telephone: 212-512-2000.
Postmaster: Send address changes to BusinessWeek, P.O. Box 8418, Red Oak, IA 51591-1418. Canada Post Publication Mail Agreement Number 40012501. Return undeliverable Canadian addresses to DHL Global Mail, 355 Admiral Blvd-Unit 4, Mississauga, ON L5T 2N1. Email: bwkcustserv@cdsfulfillment.com
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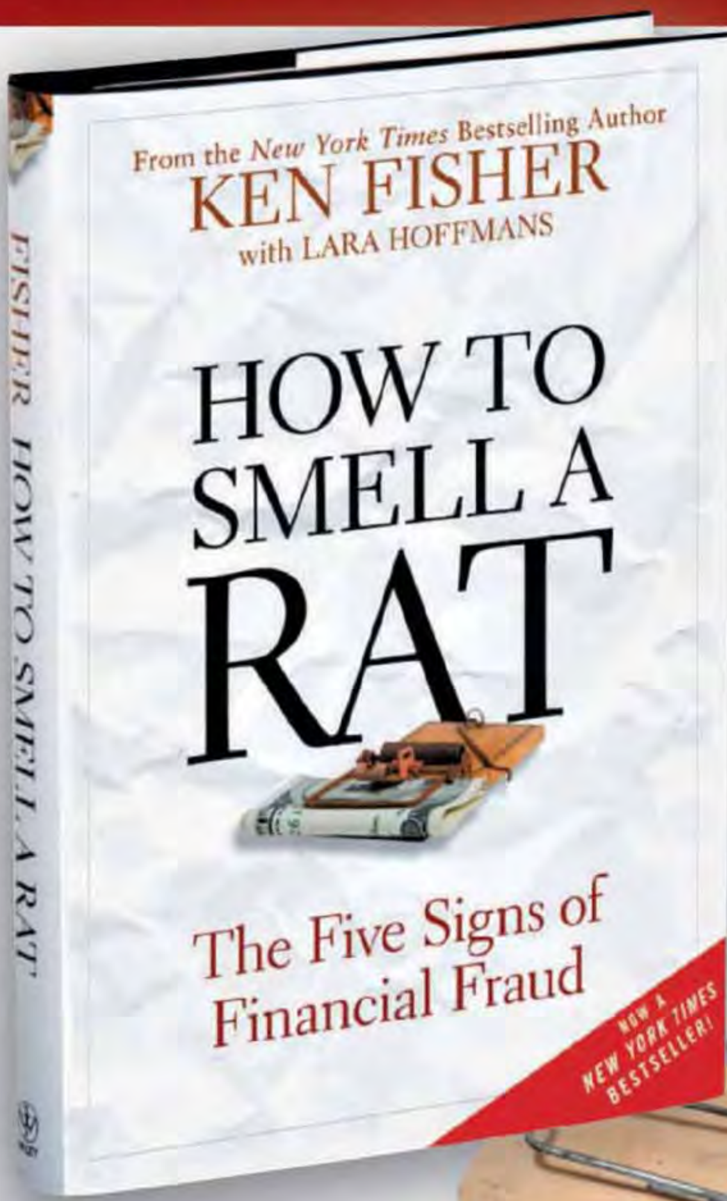
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Putting America Back to Work

Why the U.S. faces a jobless recovery and what can be done to change that

Fifty years ago the Soviet launch of Sputnik led to a national commitment to strengthen U.S. science and technology and put a man on the moon. That shift in priorities and the impressive results inspired a new generation of innovators—people such as Bill Gates, Steve Jobs, and Arthur Levinson—to create Microsoft, Apple, and Genentech. The companies they built created tens of thousands of jobs and revolutionized American industry.

Today the U.S. is facing a much more ominous event: the loss of 7 million jobs, double that of any recession in our lifetimes. This isn't just a short-term problem; it's indicative of structural flaws in our economy.

Economists are telling Americans a recovery is under way. It's true that government investments of nearly $2 trillion have saved Wall Street from collapse and that both the financial sector and corporate profits are bouncing back. But what about Main Street, where the jobs crisis gets deeper every day?



The Bureau of Labor Statistics reports that 16.8% of Americans are unemployed or underemployed, including those who have stopped looking. These statistics are much worse among Americans under 25, a quarter of whom can't find a job. For recent college grads with jobs, half are in positions not requiring degrees. Economists argue jobs are a lagging indicator. Not this time. None of the CEOs I know are hiring. Without prompt action, this recovery will be a jobless one.

The Obama Administration talks about saving jobs, but what we need to do is create them. While General Motors has emerged from bankruptcy, it is unlikely to hire more American workers. Summer construction projects and Cash for Clunkers provided short-term relief but not sustainable jobs. Much of the stimulus package has been spent on reducing state budget deficits and modest tax cuts, used by many consumers to pay off massive debts.

Instead of clinging to yesterday's economy, we should use this opportunity to rally around the cause of making the U.S. fully competitive. But what will it take to create sustainable jobs? We need to refocus on America's great strengths: innovation, entrepreneurship, small business, and new company formation. These were the engines that drove job growth in the 1980s and '90s. We can do it again by unleashing these powerful forces.

The biggest job creators are small businesses and companies that are expanding, like my former company, Medtronic, which has created 35,000 jobs in the past 25 years. Yet our national policies, unlike those in many European and Asian nations, often work against them.

One lever for creating jobs is the tax code. Imagine the surge in new businesses if tax credits for long-term investments were raised. And what if R&D tax credits were raised and made permanent? President Barack Obama had a great idea back when he was campaigning: offer a one-time capital-gains tax holiday for investors in new companies, or make capital gains taxable on a sliding scale so that they decline the longer an investment is held.

The U.S. already puts an emphasis on research spending. But now's the time to double down, especially in renewable energy, information technology, and health care—three of America's greatest strengths. And with so many workers who lack the skills for tomorrow's jobs, we should institute massive retraining and education programs to prepare workers for the high-tech jobs where the U.S. has a competitive advantage.

But this commitment to jobs has to extend beyond the government. The great job creators of the past decades—companies such as Google, Wal-Mart, Microsoft, Intel, Amgen, and Starbucks—are all innovators. Today's CEOs and venture capitalists can inspire future entrepreneurs to create the companies and the jobs that will revitalize the U.S. That's what PepsiCo CEO Indra Nooyi (page 51) has been doing by moving her company into healthy foods and beverages. Venture capitalist John Doerr of Kleiner Perkins Caufield & Byers is investing in dozens of startups in renewable energy. CEOs Eric Schmidt of Google and John Chambers of Cisco Systems continue to invest in emerging info tech companies.

Almost 50 years ago, John F. Kennedy seized the moment and declared an audacious goal. President Obama has a chance to offer a similar challenge to tomorrow's entrepreneurs—and to give them a clear shot at the target. | BW |

Bill George, professor of management practice at Harvard Business School and the former chairman and CEO of Medtronic, is the author of 7 Lessons for Leading in Crisis.

Jack and Suzy Welch are off while Jack recovers from a back infection.

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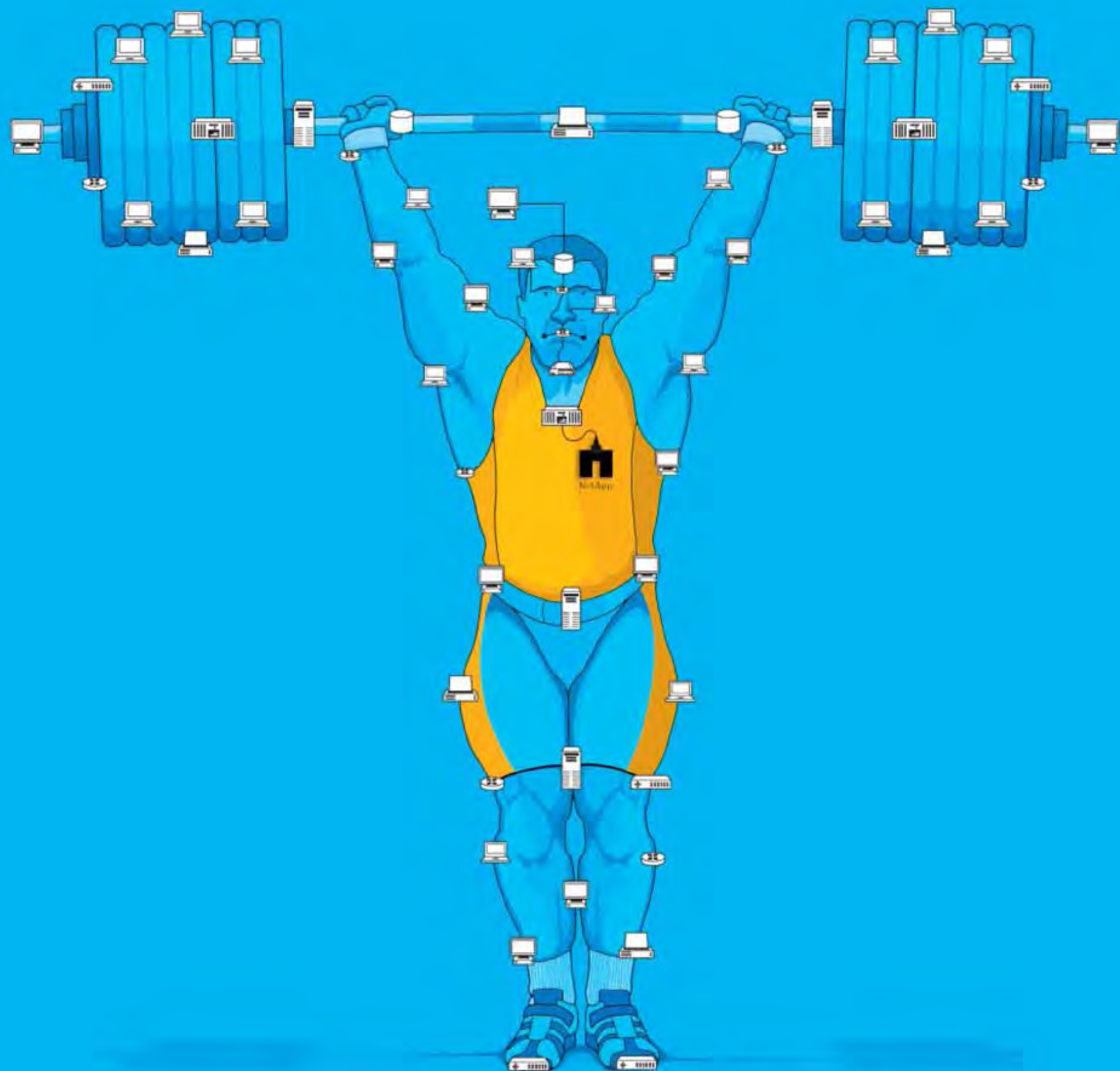
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